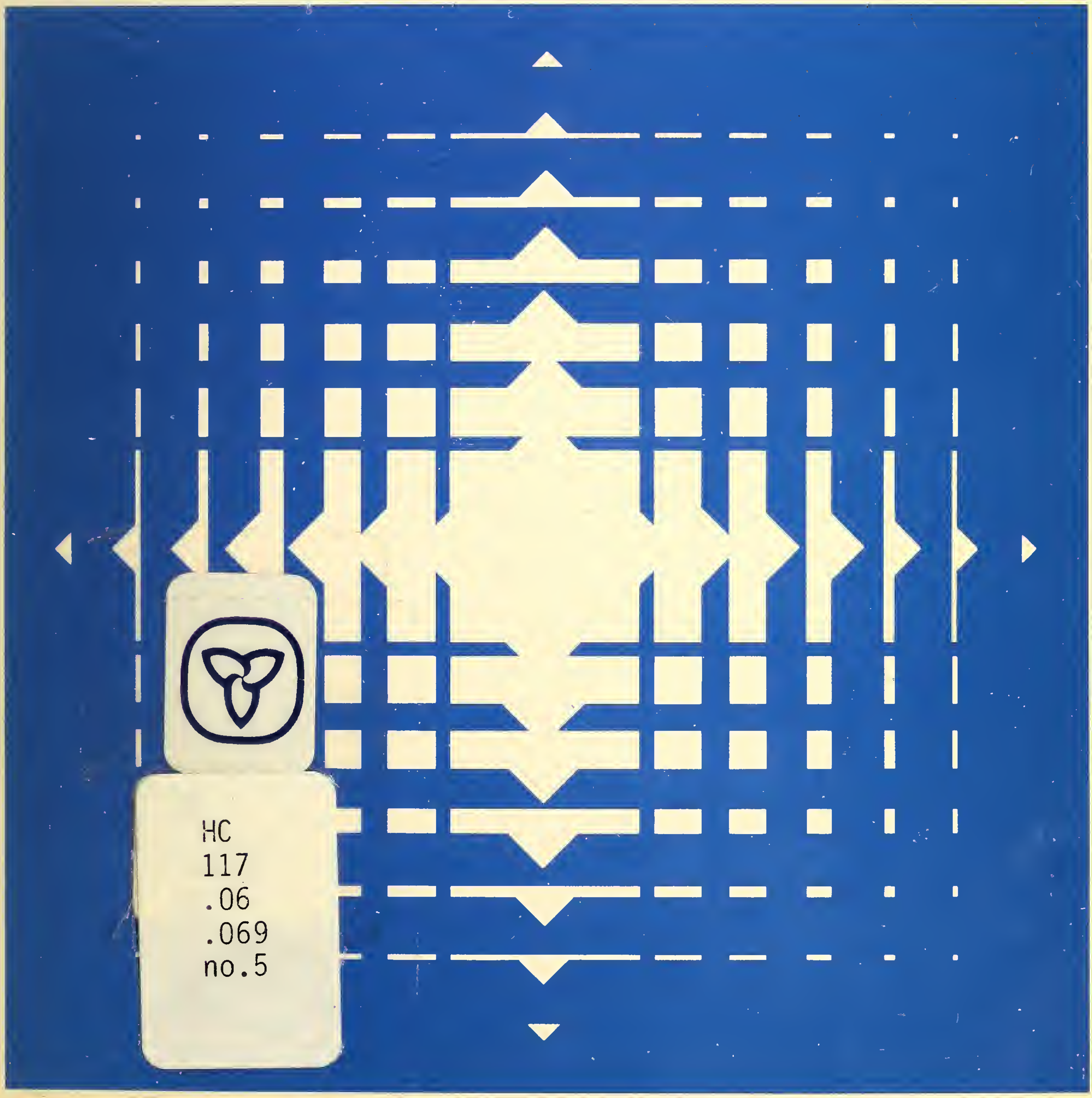
D.G. HARTLE

A Theory of the Expendi Budgetary Process

ONTARIO ECONOMIC COUNCIL RESEARCH STUDIES



A THEORY OF THE EXPENDITURE BUDGETARY PROCESS

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PUBLISHED FOR THE ONTARIO ECONOMIC COUNCIL BY
UNIVERSITY OF TORONTO PRESS
TORONTO AND BUFFALO

Library of Congress Cataloging in Publication Data

Hartle, Douglas G

A theory of the expenditure budgetary process.
(Ontario Economic Council research studies)
1. Expenditures, Public. 2. Budget. 3. Program budgeting. I. Title. II. Series: Ontario Economic Council. Ontario Economic Council research studies.
HJ7451.H36 351'.722 76-25827
ISBN 0-8020-3341-5

This study reflects the views of the author and not necessarily those of the Ontario Economic Council

Contents

Introduction

This paper has four objectives: to review the theoretical literature dealing with the expenditure budgetary process; to outline a concept of individual self-interest that is both less narrow and less vague than the concept advanced by some of the most promising theorists in the field; to set forth an alternative theory of the budgetary process; and to point out some hypotheses that can be derived from the alternative theory and might be tested, albeit in a non-rigorous manner, through case studies of the way in which particular budgeting decisions were reached.

It is acknowledged, with regret, that none of these four purposes has been fully achieved. Even the review of the theoretical literature - a seemingly pedestrian task - is limited essentially to the works of a relatively few outstanding economists. The writings of political scientists, accountants, and management-organizational experts has been largely ignored. This neglect in part arises because of the biases of the author, who is convinced that economists are on the verge of saying something extremely important about political decision-making in general and the budgetary process in particular, but also because an encyclopaedic summary would be the work of years, not months, and is probably beyond his competence. From what we know of some of the writings of political scientists, such as Theodore Lowi, they have much to contribute to the analysis of the budgetary process. Indeed, much that is contained here, although subjectively new to the author, may well have been anticipated by such writers.

The review of the literature, limited though it is, strongly suggests that what we have called the self-interest group theorists have the most insightful things to say about the budgetary process. They emphasize to varying degrees the enor-

mous importance of uncertainty (ignorance), strategic behaviour, property rights, decision rules, and implicit incentive systems. The one concept that ties them together is the concept that decision-making theories should be based on the postulate that all of the actors in the process - politicians, bureaucrats, interest-group leaders, journalists, and voters - seek their own individual interests in a rational fashion. This approach may be contrasted with others that assume, implicitly or explicitly, that a governing party or the cabinet has somehow not only defined all of the objectives of a society but also assigned relative weights to them on some kind of permanent basis. This is equivalent to the assumption that every nation is being governed by an all-knowing, stubborn, but perhaps benevolent dictator. This notion that there is what economists have come to call a 'social welfare function' has proven to be an elegant but rather empty abstraction, for in essence it denies the existence of, or at least assumes away the problems associated with, the reconciliation of the conflicting interests of individuals and groups.

For these reasons chapter 2 is devoted to a detailed definition of the concept of individual self-interest. An attempt is made to show that the concept of individual self-interest used by economists is *not* inconsistent with some of the concepts used by political scientists (power and influence) or sociologists (self-esteem and status). The general implications of this more general concept of individual self-interest are then elaborated in the concluding section of chapter 2.

Methodological purists find that analogies are anathema. They are able to show, often with compelling evidence, that false analogies are a source of many logical errors. Despite these wise injunctions, the author attempts in chapter 3 to develop a crude theory of the budgetary process based on drawing analogies between the behaviour of players in what are called 'games' in common parlance and the behaviour of politicians, bureaucrats, special interest-group leaders, and journalists, both within their own games and in a perpetual playoff series among them - the expenditure budgetary process.

The main points made in this, the third chapter, are that the players in each game seek their self-interest within the unique set of rules constituting the incentive system of their game; that it is only by changing these rules that the behaviour of the players is likely to be changed; that because obtaining information and exercising influence are costly, most voters find it prudent to play a passive role - the expected benefits do not exceed the expected costs of obtaining them; and that politicians are careful to spread costs as widely as possible while concentrating benefits on swing voters in swing ridings. Similar comments are made about the rules that affect the behaviour of bureaucrats, special interest-group leaders, and journalists.

It is frankly acknowledged that the delineation of the several games is incomplete. In particular, what is required is an analysis of the rules that affect, if they do not determine, the selection of players in each game and the rules for changing the rules of the games. For those who wish to change the outcome of the budgetary process these are probably the crucial questions.

The final chapter states, in a most tentative fashion, a few hypotheses about expenditure budgeting derived in a non-rigorous fashion from the theory developed in chapter 3. As one might expect, the call is for further research - case studies of particular expenditure decisions. Although this is a difficult task because of government secrecy, there seems no other way of gradually moving towards a greater understanding of expenditure budgeting, although it would be foolish to suppose that greater understanding would allow us reliably to predict government policy in this area. Because this is the stuff of which history is made, our failure to foretell the future may be just as well!

The last two chapters are virtually in point form. There are two reasons for the adoption of this style (or lack of style!). The first reason is that the scope of the issues is so vast that to do it justice using the traditional forms of exposition would require not a brief study, such as this, but a shelf of books. Indeed, shelves of books on political, bureaucratic, and related decision processes have already been written. The second, and major, reason for adopting point form in these chapters is that it fairly reflects the tentative and preliminary nature of the material presented. It provides a constant reminder to the reader (and probably a constant source of irritation too!) that what is being provided is a sketch of a model, not detailed working drawings. The sketch provided is only a beginning. Perhaps, however, this sketch will induce others to tackle the difficult but fascinating problems which it seeks to address. For my part, I intend to refine and extend the basic ideas presented so that the next version will, with luck, be both more comprehensive and comprehensible. Any help, including non-constructive criticism, will be gratefully received.

POSTSCRIPT

Since this paper was completed some funds have been obtained from the Laidlaw Foundation to finance a start on the case studies on policy-making alluded to in the last paragraph. Simon Reisman has agreed to work with the author in describing the process by which the federal budgets between 1969 and 1975 were formulated. Other cases will follow.

A THEORY OF THE EXPENDITURE BUDGETARY PROCESS

1

Conceptual approaches to the expenditure budgetary process

The economic literature dealing with public expenditure is voluminous. A recent standard work on the theoretical aspects of the subject (Burkhead and Miner, 1971) cites about three hundred authors. Most of them have written more than one article or book. There are, of course, thousands of more obscure authors who also might have been cited. However, only a relatively small fraction of this literature is concerned directly with the subject matter of this paper: the decision-making process. Indeed, a substantial part of the public expenditure literature, particularly the most theoretically sophisticated and elegant part, is based on assumptions that make the decision-making process irrelevant. It may be useful briefly, and hence crudely, to summarize the field in order that the reader may better understand the current status of that small segment of the literature that is of immediate concern.

GRAND THEORIES

There are several 'grand theories' that purport to explain the growth in the relative size of the public sector. The most important of them are described, analysed, and evaluated in Bird (1970). Because this study is readily available there is no need to recapitulate in detail what Bird says, particularly because he found, as have we, that most of these grand theories are not of much help. A brief summary of Bird's work may, however, provide a useful perspective.

Wagner's Law

Adolph Wagner, a German economist who wrote extensively over a hundred years ago, formulated a 'law of expanding state expenditures' as an inevitable

consequence of the 'progressive' state – where the state was conceived of as an entity that had a will of its own apart from the tastes and preferences of the individual citizens who comprised it. Although not expressed either in rigorous or objectively measurable terms, Wagner's Law suggested that an increase in the relative size of the public sector would arise because of rising per capita incomes, which would induce greater spending on cultural and welfare programs; greater complexity of legal relationships and communications resulting from an ever more elaborate division of labour; increased problems associated with urbanization; and increased state intervention in the economy because of increases in the optimal size of industrial facilities.

After a review of the literature and some statistical data, Bird concludes that 'on the whole, however, the evidence, such as it is, must be considered mildly favourable to Wagner's "law"' (Bird, 1970, 75). The question is whether or not the law is useful in helping us understand the growth in public expenditures in Canada? Bird's answer is a clear no. 'Wagner's "law" may help illuminate some aspects of past reality, but it would be myth-making of the worst sort to contend it has anything useful to tell us about the future' (ibid., 81). The reader should consult Bird's book for the thoughtful analysis underlying this conclusion. It should be noted in passing, however, that Wagner was not concerned with the budgetary decision-making process as such. His organic view of the state neatly sidesteps the whole question because 'the state' acts for its 'own' reasons. The problem of reconciling the conflicting interests of voters and bureaucrats is, in a sense, assumed away.

The demand for public services

One of the most common explanations of the growth in government expenditure is that the goods and services provided by governments are, in a sense, luxuries. The higher are personal incomes, so goes the argument, the larger is the fraction of it individuals want to spend on them. To put the proposition in more technical language, the demand for public goods is highly income-elastic. The trouble is that this is more a description than an explanation of reality. Why do individuals want to spend an ever increasing proportion of their incomes on health and educational services as their incomes rise? Indeed, do the relative increases in these kinds of government expenditures reflect changes in individual wants or are some other factors at work? Does the process of cumulative decision-making simply translate these changes in individual wants into government programs? If so, how? Or does the process somehow or other produce results that are at least partially independent of individual wants? If so, how and why?

Bird's conclusion to his discussion of this approach is well worth quoting:

To sum up, the notion of the income-elasticity of public expenditures, although it occurs frequently in the literature, is singularly barren of fruitful hypotheses 'explaining' in any meaningful sense the growth of public expenditures. One thing *is* made clear by this discussion, however ... a disaggregated approach to public expenditures is necessary if our aim is to understand what is going on. Another is that the individualistic approach to the positive analysis of public expenditures, like the organic state approach, is inadequate, although it has the considerable advantage over the latter in that *it makes clear the need for explicit analysis of the dynamics of the political and administrative process* (ibid., 96).

The supply of public services

Bird describes and analyses four theories in his chapter devoted to this topic: productivity lag, tax limit, the displacement, and revenue structure (ibid., 97-117).

The productivity lag theory hinges on three propositions: labour productivity rises more rapidly in the production of goods than of services; a much larger fraction of the output of the public sector than of the private sector is made up of services; because of measurement problems the output of the public sector is measured in terms of inputs, so that there are no measured productivity increases by definition. This means that if, over time, the ratio of inputs into the public and private sectors were held constant, the output of the public sector would appear to become an ever diminishing fraction of total output. It also means, however, that if the public sector share of total output is to remain unchanged, the inputs into the public sector must be constantly increased relative to those going into the private sector to offset the measured productivity increases taking place in the latter. This theory, therefore, explains away a part of the increase in the size of the public sector as a statistical illusion and another part as a result of the differential impact of changing technology on the production of goods relative to services. It is, however, essentially vacuous because changes in the productivity of many factor inputs in the public service are not measurable.

The tax limit theory, as its name suggests, is based on the idea that there is some ultimate ceiling on government expenditures that is reached when taxes (rates? share of GNP?) become 'too high.' This approach is both vague (Does it not matter how the revenues are spent?) and incomplete (What is the mechanism by which the feedback occurs? What happens when the ceiling is reached?). Despite its obvious intuitive appeal, the tax limit approach, at least as presently formulated, has little to offer. Like the productivity theory, the limit theories do not take the decision-making process into account.

The same is true of the displacement theory, which attributes increases on public expenditures to wars and similar upheavals (e.g. world-wide depressions).

Having raised taxes to fight a war, non-military expenditures expand to fill the room created by the maintenance of tax rates and bases and by the reduction in defence expenditures at war's end, according to this view. Expenditures therefore rise dramatically to a new plateau, remaining relatively constant until the next disaster, when they rise quickly again. This theory does not explain why the public demand for additional expenditures is suppressed during interwar periods, nor why voters and/or politicians and/or bureaucrats do not cut taxes, rather than increase expenditures, when the war or similar disaster is over. The displacement theory does not encompass a theory of fiscal psychology that might be incorporated into a theory of the budgetary process, although it implies one.

The tax structure theory goes something like this: a given increase in national income generates different rates of increase in revenues depending on the structure of the tax system. Those structures with high income elasticities yield greater increases in revenues as national output rises than do structures with lower income elasticities. There is no doubt that the continuous automatic increases in revenue that occur because of income-elastic tax systems are *politically* less painful than additional revenues raised by explicit increases in tax rates or tax bases. Presumably, the more income-elastic the tax system, the faster expenditures tend to rise relative to less income-elastic tax systems. But, as Bird points out, this does not necessarily mean that the rate of increase in expenditures is *governed* by the elasticity of the revenue structure. 'The bulk of the available evidence appears to indicate that the existence of a revenue constraint, at least in an organized state with an adaptable administrative machine, has not up to now been a long-run barrier to expanding government spending' (ibid., 119).

It is undoubtedly true, as Bird says, that even during relatively tranquil periods governments do raise tax rates and broaden tax bases. The rate of increase of government expenditures is not rigidly constrained by the rate of increase in revenues produced by ever higher incomes and the same rates and bases. The more interesting question is the extent to which the automatic increases in revenues tend to create a lower limit below which the rate of increase in expenditures rarely falls. There *have* been some tax cuts, particularly at the federal level, during recession periods. The lower limit obviously is not rigid either. But it is hard to believe that expenditures would be so high as they now are in Canada if the tax system had zero income elasticity. Unfortunately, here too, the theory has little to offer because the issue is more closely related to fiscal psychology and the budgetary process about which it is silent.

In summary, it seems fair to say that the grand theories discussed by Bird provide some useful insights but, with the exception of Wagner's Law, are more partial descriptions of what happens in the real world than explanations of it. None

of these theories attempt to deal with the decision-making process that forms the link between the changes in the wants of individuals and the changes in government expenditures that either satisfy or frustrate these wants.

THEORIES OF MARKET FAILURE

The whole body of literature known as welfare economics that has developed since the mid-1930s is concerned with the problem of defining the conditions under which private markets fail to provide an efficient allocation of resources and therefore require state intervention, including public expenditures. An efficient allocation of resources is defined as one where nobody can be made better off (level of personal satisfaction increased) without making somebody else worse off (level of personal satisfaction reduced).

Such an efficient allocation of resources is termed 'Pareto-optimal' after the Italian economist who first expounded it as a criterion. Generally speaking, the concept of Pareto optimality usually assumes an initial distribution of property rights (that is, assets or the income flowing from assets) that is in some sense satisfactory. It also explicitly assumes that each individual's level of satisfaction is independent of the levels of satisfaction of others. Further, those using the concept usually implicitly assume that individual satisfaction is derived solely from the consumption of tangible goods and services. Clearly, under the first of these three conditions the concept of Pareto optimality cannot be used to assess policies that try to change the distribution of income among individuals.

An attempt has been made in recent years to eliminate this limitation by assuming that individuals have what might be called a propensity to be 'benevolent' and gain personal satisfaction for themselves by increasing the satisfaction of others through voluntary transfers to them. However, this formulation is not without its problems. First of all, while conceivably a voluntary transfer from A to B increases the satisfaction of both, it is possible that C is jealous of B, so that his satisfaction declines – with the result that the transfer is not Pareto-optimal.

Secondly, it is possible that, while A, B, and C would all gain satisfaction if B received a voluntary transfer, if the increased satisfactions of both A and C were contingent upon the size of the contribution of the other, Pareto optimality could not be achieved unless they both agree to act in concert in a specific way. This immediately raises the issue of strategic behaviour, with each one jockeying to pay a smaller share. As explained later, only if the members of the group unanimously agree to act can one be certain that no one is being made worse off by the redistribution. It seems reasonable to assert, therefore, that the Pareto optimality rule, except under some highly special circumstances, cannot cope, even conceptually, with the evaluation of redistribution policies.

The most important insight of welfare economics, from the point of view of public expenditure, is the concept of externalities (also known as 'spillover effects,' or 'third party effects,' or 'non-appropriability'). An externality exists when one individual's production or consumption or behaviour bestows on others *either* favourable effects (benefits) from which they cannot be excluded if they do not pay *or* unfavourable effects (costs) which they cannot charge back to the person generating them. Smoke pollution is thus an example of a negative externality. Given that each individual follows his self-interest, private markets will result in too little production and consumption of goods and services that yield positive externalities and too much production and consumption of goods and services that yield negative externalities. That is to say, if governments could increase the production and/or consumption of goods and services with positive externalities, either through subsidies or government provision, at least some individuals would be better off and none would be hurt; the converse also holds for the imposition of taxes or regulations that would reduce the production or consumption of goods and services with negative externalities. It should be noted, however, that 'better off' and 'worse off' are here being defined in accordance with a stringent (narrow) concept of Pareto optimality. It should further be noted that it is assumed that the measures adopted to deal with the externalities, such as public provision, do not themselves create distributions that give a worse net result (again in Pareto-optimal terms) than continuing to live with the problem. For example, the taxes used to finance the public provision of a good or service needed to correct for a positive externality might induce some individuals to consume more leisure and fewer private goods than they otherwise would. This loss may not be offset by the gain they obtain from the additional public good.

There has of course been an extensive controversy, particularly in recent years, about the 'true' nature or cause of externalities and the appropriate way to deal with them. Of particular importance for our purpose is the emerging view that transactions costs and preference revelations are the heart of the matter. Transactions costs are defined to include such things as the costs of information, communications, enforcement of rights, and negotiating costs. Preference revelation means the willingness or unwillingness of individuals to divulge how much they value something. Those who can enjoy a 'free ride' are unlikely to be willing to divulge how much they value it if they were to be charged accordingly. The unwillingness of an individual to reveal his preferences may be thought of as a situation where marginal information costs are infinitely high.

The point is simply this. If transactions costs were zero, property rights could exist in all scarce resources (e.g. pure water and air, privacy, and so on). Those who used them (made them even more scarce) could be required to pay for the

benefits received because the information would exist about who was using what. Charges could be levied accordingly by those owning the rights. This would take care of the overproduction and/or overconsumption of goods and services with negative externalities. Similarly, if transactions costs were zero, perfect information would be available about how much everyone valued everything. Quality standards could be specified and enforced without controversy. Those who refused to pay for what they enjoyed could be readily excluded from the source of the benefit. Private suppliers could negotiate separate contracts with millions of people. As long as governments maintained property rights, suppliers would be able to charge all of the beneficiaries for all of their benefits. The problem of undersupply or underconsumption because of positive externalities would disappear and efficiency would be improved.

It does not follow, of course, that where there are transactions costs, governments must necessarily step in and either subsidize or provide goods and services. Transactions costs are ubiquitous. They exist in all modes of economic organizations, private and public. What does seem to follow is that at least some of the functions of governments are derived from an unlikely source, a lack of information, because it is either too costly to obtain or inherently unobtainable in the public sector (such as a knowledge of individual tastes and preferences).

THE PURE THEORY OF PUBLIC EXPENDITURE

The pure theory of public expenditure deals largely with the most extreme form of market failure, pure public goods. As indicated above, these are goods (and services) such that they are necessarily simultaneously supplied to groups of individuals, the benefits enjoyed by one such individual do not diminish those of others, and those who do not pay for them cannot be excluded, so that free riders refuse to reveal the value they place on what they get. The maintenance of national security by a military force is the usual example; the chiming clock in the tower of the town hall is another; a more 'equitable' distribution of income is still another (although this is more controversial).

Two streams of thought about pure public goods are of interest to us. One stream has sought to define the conditions under which particular public goods would be supplied in Pareto-optimal amounts, assuming, in addition to the three assumptions already stated, that their provision would not affect relative prices. Part of this stream ignores the problem of preference revelation and concentrates on the derivation of the logical consequences of hypothetical 'facts' about individual tastes and preferences and production costs. This is not an intellectually trivial task, but the same cannot be said for its operational significance!

Another part of the first stream does not assume away the problems of preference revelation. It basically comes to the conclusion that where goods necessarily bestow benefits on large groups, and exclusion cannot be enforced, government provision is a necessary, but not a sufficient, condition for the achievement of an optimal allocation of resources. Where small groups are involved it is possible that private collective provision (e.g. by a voluntary association) may be feasible, because the members can bargain with one another about the allocation of the costs. When the group is small enough the share of each is a significant part of the total, so that potential free riders recognize the possibility of non-provision if they show an unwillingness to contribute. However, even in the small-group case, the outcome will depend on the relative bargaining power, strategic skills, and quality of information of the parties. There is therefore no reason to believe that the outcome will be optimal.

Another stream of thought in the pure theory of public expenditures assumes the existence of what has come to be called a social welfare function. This function specifies the standard against which to judge the merits of all possible combinations of all public and private goods and all possible distributions of these goods among individuals. Given this hypothetical standard it is possible to specify the theoretical conditions under which optimal social welfare can be obtained. The problem is, of course, the lack of operational content for the concept of the social welfare function.

Kenneth Arrow (1951) has shown that, except under extremely stringent conditions, it is not possible to derive a social welfare function from the aggregation of individual preferences, expressed through voting or similar procedures, when these preferences differ between individuals, except within narrow limits or by accident. This means, in effect, that achieving an optimal result, defined in accordance with a social welfare function, probably implies a degree of coercion. There would be absolute losers, contrary to the Pareto optimality rule. This in turn implies that someone, somehow, has decided that an increase in the social welfare of A and B is sufficiently meritorious to warrant the reduction in the welfare of W and X that was necessary to achieve it.

But what legitimacy has a particular social welfare function? Presumably if such a function were set forth by legitimate authority (the cabinet, say, of a duly elected democratic government) it would be legitimate enough for the purposes of a public servant who was advising that authority. Whether or not that degree of legitimacy would be sufficient to induce the losers to acquiesce in their losses is another matter. But economists have not concerned themselves with these questions. Even Arrow, and those who have followed in his footsteps, have been concerned solely with the problems in logic of aggregating divergent individual tastes and preferences through voting or similar procedures. Scant atten-

tion has been paid to the questions of the institutional framework within which such voting might occur, or the incentives that would have to prevail to induce the actors to engage in such an exercise.

In both streams the pure theory of public expenditure can be looked upon as an attempt by economists to make normative statements about public policy that are true by definition if no mistakes in logic have been made. By assuming that there would be unanimous acceptance of a policy change that made some better off and no one worse off,[1] and by assuming that individual tastes and preferences are known, it is possible to deduce what should be done. On the other hand, those who posit the existence of a well-defined social welfare function that serves as *the* standard by which to judge all possible policy changes either assume that this is simply a reflection of individual preferences about which there would be unanimous agreement (an unlikely outcome if Arrow is correct) or simply a standard established by God or a benevolent dictator or 'duly appointed authority' which would establish the extent to which one man's interest should be sacrificed to the interest of another.

This is not to say that the pure theory of public expenditures has not been without value. It has provided an elegant rationale for certain kinds of government expenditure (pure public goods); it has clarified complex logical relationships that can perhaps serve a useful positive purpose; it has made clear that economists, or technocrats, can say little, if anything, about the merits of alternative government expenditures except in terms of criteria provided by others. But having said all this, it seems hard to deny that the pure theory of public expenditures in particular, and welfare economics in general, has little to contribute to an understanding of the expenditure budgetary process except to emphasize that, in the absence of either preference revelation or social welfare functions descending from on high, the *process* is of vital concern. Indeed, it is one of the major themes of this paper that the over-all political process, and the budgetary process within it, is a means by which the political-social-economic system copes with the *absence* of the kinds of information, including evaluative criteria, that the theories just discussed assume to exist.

SELF-INTEREST THEORIES OF COLLECTIVE DECISION-MAKING

An extremely interesting and potentially important development has taken place in recent years. Members of a small group of economists have begun to turn their attention, and analytic tools, towards the development of theories of politics. Of

1 This implicitly assumes that unanimity is the decision rule adopted for government.

particular interest are the works of Anthony Downs, James Buchanan, Gordon Tullock, Mancur Olson, William Niskanen, and Albert Breton.[2]

All of these authors have one thing in common: they seek to explain collective decisions (about what are often thought to be political matters) in terms of the self-seeking behaviour of rational individuals. They are thus mining that rich intellectual vein first discovered by Adam Smith, the vein that essentially sets forth two propositions: a great deal of individual behaviour can be explained (e.g. predicted) if we assume that most people most of the time are seeking to maximize their own welfare; given 'appropriate' institutions, such as markets, the boundless energy that drives people to seek their own selfish advantage can be harnessed to achieve socially desirable ends. To quote again the most quoted sentences in *The Wealth of Nations*: 'It is not from the benevolence of the butcher, the brewer or the baker, that we expect our dinner, but from their regard to their own self interest. We address ourselves not to their humanity but to their self love, and never talk to them of our own necessities but of their advantages' (Smith, 1937, 14).

Albert Breton (1974) probably has come closest to the provision of an integrated, coherent general theory of collective decision-making based on the self-interest postulate. But, as the subsequent summary and evaluation of it attest, there is still some distance to go. The reader is more likely to appreciate the strengths and weaknesses of Breton's work after a review of his modern predecessors.

Anthony Downs

Anthony Downs (1957) is concerned with the analysis of the behaviour of a number of hypothetical political parties vying with one another for office in a hypothetical democratic government and the behaviour of a multitude of hypothetical voters each of whom vote for the party they think will best serve their interests.

A political party is defined as 'a team of men seeking to control the governing apparatus by gaining office in a duly constituted election' (Downs, 1957, 25). It is assumed that all members of a party share precisely the same goals and that 'they act solely in order to attain the income, prestige, and power which come from being in office. Thus politicians ... never seek office as a means of carrying out particular policies; their only goal is to reap the rewards of holding office *per se*' (ibid., 28). Policies are a means to office; office is not a means to policies in this formulation.

2 It should be acknowledged that there were precursors: Wicksell and Lindahl and Musgrave in particular.

Each voter, in the Downs model, is assumed to maximize his 'utility income from government activity' (ibid., 38). This strange term encompasses all the net benefits from government, whether perceived by the voter or not, and can include the pride derived from being a citizen of a country whose government gives aid to non-residents. Altruism is therefore not ruled out; it is charity motivated by the personal satisfaction it gives the donor.

Having defined the characteristics of the principal participants he then goes on to explain voting behaviour in terms of the voter's expected net benefits from casting his vote among the alternative competing parties. In discussing the strategies of the political parties designed to capture the largest number of votes he first deals with a situation where there is certainty (perfect knowledge). He summarizes his findings as follows:

According to our hypothesis, governments continue spending until the marginal vote gain from expenditure equals the marginal vote loss from financing. The determinants of vote loss and vote gain are the utility incomes of all voters and the strategies of opposition parties. Thus governments are engaged in political warfare as well as maximization problems. Under conditions of certainty, a government's best strategy is to adopt choices which are favoured by a majority of voters. Before making any expenditure, it takes a hypothetical poll to see how voters' utility incomes are affected ... If it fails to adopt the majority's views, its opponents will do so and will fight the election on this issue only, thereby insuring defeat for the incumbents (ibid., 73).

After discussing the possibility of a coalition of dissenters, he later concludes: 'Since governments plan their actions to please voters and voters decide how to vote on the basis of government actions, a circular relation of mutual interdependence underlies the functioning of government in a democracy' (ibid., 74).

Unlike most writers on the subject, Downs devotes more than half of his book to dealing with the consequences of uncertainty, which he defines as any lack of sure knowledge about the source of events. The existence of uncertainty creates a role for persuasion (the provision of correct but biased information). As soon as there is a role for persuasion there is a role for leadership within and among political parties, interest groups, and favour-buyers. Uncertainty within a government also creates a role for intermediaries who seek to interpret the views of the voter to the government, and vice versa. These intermediaries (members of the party, the bureaucracy, interest groups, and favour-buyers) 'exact a price for which they get an influence over policy formations greater than their numerical proportion in the population ... [which] modifies the equality of influence which universal sufferage was designed to ensure' (ibid., 95).

Uncertainty, in Downs's view, also is the raison d'être of ideologies that voters use to reduce their information costs and parties use to attract the support of groups of individuals who vote for general ideologies that appear consistent over time (and with past performance), appeal to the largest number of voters, and yet differentiate each party from its competitors. He concludes that when there are two parties they will tend to converge on the ideological centre, but that fear of losing extremist voters will keep them from becoming identical. He also has interesting things to say about the special attributes of coalition governments.

The problems of attaining, through government policies, Pareto optimality in a world with externalities and pure public goods is discussed at considerable length by Downs. He emphasizes that when uncertainty exists, as it surely does, Pareto optimality would not be achieved by the market even in the absence of these two impediments. He then goes on to say that in an uncertain world it would only be by chance alone that governments would take those actions necessary to achieve an optimal allocation of resources. Among the factors contributing to this negative outcome are the unequal distribution of influence biased in favour of high income individuals, the unique coercive power of governments, the impossibility of increasing the benefits all individuals receive from government, given differences in their preferences or their innate abilities, and the illegality of selling votes.

In this part of his work Downs reaches two conclusions of particular concern to us. The first is that while there is always a tendency of a vote-maximizing democratic government to redistribute income from rich to poor because the former are obviously less numerous than the latter, this is offset by the greater political power of high-income groups, owing to uncertainty – uncertainty about the disincentive effects of redistributive policies, for example. His second conclusion is that, because governments allocate expenditures so as to equalize the votes obtained at the margins rather than the social benefits (e.g. voter utility), there will be widely divergent rates of return, as measured by cost/benefit analysis, among government activites, a situation that could not long prevail in competitive markets.

It is not possible in a brief space to summarize in any detail the last two parts of his book, which are concerned with information costs and derivative implications and hypotheses. The following quotations perhaps convey the essence of his argument:

Even if men received the same amount of data, not all could use it with equal efficiency. In fact, the divisions of labour and the presence of uncertainty guarantee that rational men will be politically informed to different degrees. Thus the foundations for inequalities of power are inherent in democratic societies, even though political equality is their basic ethical premise (ibid., 237).

If he [the voter] is going to exercise any influence at all, he must limit his awareness to areas where intervention pays off most and information costs least. These are the areas of his production specialization, since his income flows from them and he already knows a great deal about them (ibid., 258–9).

James Buchanan and Gordon Tullock

The *Calculus of Consent* (Buchanan and Tullock, 1962) appeared five years after the publication of Downs's treatise. However, both authors had published or privately circulated material dealing with several of the same issues prior to Downs's book. It appears that all three came to roughly the same conclusion independently: it is possible to explain many political decisions by assuming individual self-interest.

The *Calculus of Consent* is subtitled 'The logical foundation of constitutional democracy,' and the bulk of the book is concerned with 'the calculus of the rational individual when he is faced with questions of constitutional choice' (ibid., vi). By constitutional choice the authors mean the selection of the set of 'rules that is agreed upon in advance within which subsequent [collective] action will be conducted' (ibid., vii). The word 'constitution' is therefore given a broader meaning than is customary; for, in principle, it applies to the decision rules under which any kind of collective decision is made.

Although the authors assert that their conclusions are equally applicable to the analysis of changes in existing decision rules, their methodological approach is to assume, at least at the beginning, that a government exists that does no more than protect humans and property rights. All other activities are carried out in the private sector. The questions they then ask are: What further collectivization is necessary? and Under what terms? It must be made clear at the outset that the authors are *not* concerned with decision rules that emerge because all members of the group share the same goals. They are interested in the more relevant case where different individuals and groups seek different things through the political process.

The reader will recall the use of the term 'transaction costs' earlier in this chapter. Buchanan and Tullock call these 'decision-making costs.' They argue, as was shown earlier, that if transaction costs were zero, an efficient allocation of resources would be achieved through private markets if the state carried out only one function - maintenance of property rights. The choice between voluntary action (individual or co-operative) and state action, is, therefore, a choice that must be made on the basis of the relative decision-making costs in each case *and* the costs of bearing the negative externality or foregoing the positive externality. That is to say, individuals will always choose the minimum decision-making cost if they act collectively; collective action will only take place, however, when the minimum decision-making cost is less than the cost of the negative externality or

the benefit of the positive externality. This is little more than saying that individuals will choose the most efficient organization, including no organization at all, if the costs of the most efficient organization are not worth the candle.

The interesting point the authors make is that when comparing the decision costs for voluntary collective decision-making relative to compulsory collective decision-making (government) the voting rule on which decisions are based is of crucial importance. Unless a unanimity rule is adopted it is virtually certain that some will be coerced. The smaller the fraction of those affected who are required to agree to a collective action the greater the likelihood that a particular individual will have to live with a collective decision that imposes a cost on him. On the other hand, the larger the required fraction the greater the costs of obtaining agreement because, in the extreme, with a unanimity rule it will pay individuals to try to hold out for a decision in which they obtain most of the benefits of the collective action for themselves. As the authors state:

The only means whereby the individual can insure that the actions of others will never impose costs on him is through the strict application of the rule of unanimity for all decision, public and private. If the individual knows that he must approve any action before it is carried out, he will be able to remove all fear of expected external cost or damage. However, as we have already suggested, he must also consider the costs that he can expect to incur through the operation of such a rule ... in groups of any substantial size the costs of higgling and bargaining over the terms of trade that may be required to attain agreement often will amount to more than the individual is willing to pay (ibid., 72).

The rule of unanimity is thus advocated by these authors as the standard against which all decision rules should be judged. It has the same significance to their argument as the concept of Pareto optimality has to welfare economists. However, the unanimity rule is certainly not identical to the Pareto optimality rule as usually formulated because it is conceivable that all individuals would agree to income redistribution if the immediate losers believed that they might be gainers, directly or indirectly, at some point of time in the future.

The main message of Buchanan and Tullock is that, despite popular opinion to the contrary, majority rule has no magic. It allows 51 per cent of the voters to coerce the other 49 per cent. Why not adopt a 75-25 per cent rule, so that where 26 per cent of the voters are opposed to a proposal they can block it? They point out that if voters were allowed to trade their votes (which goes all the way from simple logrolling to the open buying and selling of votes) 'individual intensities of preference on political issues [would be] more fully expressed. Any of these institutional modifications in the operation of voting rules

will tend, therefore, to lower somewhat the external costs that the activity is expected to impose on the individual' (ibid., 209). That is to say, under anything less than the unanimity decision rule, individuals will more readily acquiesce in a wider scope for the public sector if they know they can block changes they strongly dislike by 'buying' support for their position. Conversely, when vote trading is not allowed, presumably for ethical and legal reasons, individuals will tend to insist on constitutional provisions that more narrowly restrict the range of government activities so as to preclude being coerced.

After discussing the extent to which the use of less than full consensus rules will tend to result in an overextension of the public sector, relative to some ideal, they reach a conclusion that is particularly pertinent for this study:

The individual, in his role of constitution-maker, does not choose directly the size and the scope of the public sector, 'the allocation of resources.' Individuals choose, first of all, the fundamental organizations of activity. Second, they choose the decision-making rules ... To make normative statements concerning whether or not governments undertake 'too much' or 'too little' activity seems to be rather wasted effort *unless one is prepared to suggest some possible modification in the organizational rules through which decisions are made*, aside, of course, from the purely propagandist and non-scientific effects of such pronouncements. (ibid., 210)

With respect to pressure groups Buchanan and Tullock make the surely valid point that most discussions of pressure groups seek to evaluate them in terms of their impact on 'the public interest,' a term which cannot be defined because, like the concept of the social welfare function, it either assumes that all individuals have the same tastes and preferences (a trivial case) or that some god-like entity has somehow or other decided in whose favour conflicts *should* be resolved. In essence, they argue that one can only be certain a particular course of action is in the public interest if it is unanimously endorsed by all those affected. This implies, of course, that as one backs further and further away from the unanimity rule one can be less and less certain whether particular decisions reached by organizations are in the public interest. It follows that it is by improving decision rules and institutional arrangements that individuals are best able to ensure that the public interest, somehow defined, will be better served.

From this perspective, Buchanan and Tullock see pressure groups as 'an inherent and predictable part of modern democratic process' (ibid., 295). Under the existing majority rule it is possible for interest groups to arrange, by means of side payments, for discriminatory legislation (e.g. legislation that would not be unanimously adopted unless compensation to the losers was provided). This in-

duces other groups to organize to obtain similar kinds of advantages or protect their interests against incursions. In the authors' view:

> If, in fact, the organization of special interests had advanced to the point at which no one interest can expect, in the long run, to secure differential advantage, the way may be open for some changes in the organizational rules themselves. Each interest group will, of course, turn every effort toward improving its own position, *within the limits of the prevailing rules*; but if, in fact, all interests come to recognize that the external costs (the losses of those being coerced) involved in this continuous struggle of interests are excessive, all might agree on some changes in the rules that allow such behaviour to take place (ibid., 290).

Mancur Olson

Olson (1965) seeks to explain the existence and behaviour of voluntary organizations, largely of the pressure-group type. As with the other authors we have discussed, he starts from the assumption that each individual serves his own interest. He is concerned with analysing the circumstances under which the benefits of organization exceed (or can be made to exceed) the costs of organization, so that individuals will act collectively rather than individually in pursuit of one or more of those interests.

Olson points out that voluntary organizations, when they are successful, provide, in effect, public goods. That is to say, members of organizations share in the benefits even if they have not borne a share of the cost. Indeed, some organizations provide benefits that may be shared by members and non-members alike. Voluntary associations thus face the 'free rider' problem. Except for very small groups, where the benefit per member can be large relative to the organizational costs per member (includes not only out-of-pocket expenses but also the time and energy involved in communicating and bargaining), some kind of coercion or some form of selective incentive, other than the direct benefits of collective action, is necessary for the organization to come into being and reach optimal size. The larger the group, in Olson's view, the less likely that it will come into being or reach optimal size without these carrots or sticks. This is because of one or all of the following factors: when the 'pot' of benefits is fixed the benefit per member falls as the size of the group rises; organizational costs (as defined above) probably rise too, although not necessarily as rapidly as the size of the group rises; the larger the group the less important the contribution of a particular individual, so that he can readily rationalize a failure to participate and the less feasible it is for the organization to put social pressure on him to bear his share of the load.

Olson devotes a good deal of attention to the analysis of the behaviour of particular interest groups to test his hypothesis that coercion or selective incentives are a necessary ingredient of voluntary organizations that encompass large groups. He finds, as might be expected, that this indeed is the case. Many groups have legislation that allows them to force individuals to become members and pay fees in order to enjoy the benefits. He also finds that those lacking this power usually provide the membership with a package of benefits, such as a mixture of economic (collective bargaining), political (lobbying), and social benefits because the political benefits alone would not be sufficiently attractive to induce voluntary membership.

The point of all of this, from the present standpoint, is that some work has been done to explain the existence and characteristics of pressure groups that presumably seek, among other things, to bring about changes in the expenditure budget. It is also of importance to note that Olson's analysis strongly suggests that, because of the factors cited above, some interests are much more likely to be strongly represented than others. This inequality of representation of individual interests can be explained largely in terms of what might loosely be called economic variables.

William Niskanen

None of the theories or approaches outlined thus far give explicit consideration to the role of the bureaucracy in the collective decision-making process, nor do they deal, except in passing, with budgetary decisions which are, of course, a subset of the whole. The purpose of this section is to sketch one theory that partly fills this gap - the model developed by William A. Niskanen (1971). The reader is also directed to Downs (1966), a more general theory than the former but devoting less attention to the budget question.

Niskanen, like Downs, Buchanan, et al., uses the concept of the rational maximizer to construct his theory: he seeks to explain the budgets and outputs of bureaus as the logical outcome of the maximizing behaviour of the sponsors and managers of bureaus. Bureaus are defined as organizations where 'the owners (sponsors) and employees of these organizations do not appropriate any part of the difference between revenues and costs as personal income'; and 'some part of the recurring revenues of the organization derive from other than the sale of output at a per-unit rate' (Niskanen, 15).

A typical government department or agency is thus a bureau in Niskanen's sense, for in neither case are the 'profits' appropriated (except in the special sense that costs may be allowed to rise to absorb revenues) and the revenues do not come primarily from sales. Most voluntary associations are by this definition also bureaus; but corporations, partnerships, and sole proprietorships are not.

The primary difference between the kinds of goods and services produced by bureaus and those produced by profit-making enterprises, according to Niskanen, is that the former supply things which some people would prefer to have provided in greater quantities or higher qualities than would be supplied in the market through voluntary exchanges between buyers and sellers. He distinguishes between public organizations, which are the sponsors of bureaus, and private organizations, which may be bureaus themselves (if they are simple) or sponsors of bureaus. Membership in the former usually can only be changed through physical moves to another jurisdiction; changes in membership in private organizations usually do not impose such heavy costs (e.g. shifting from university to university, club to club, or church to church).

In commenting on why some goods in services are provided by private enterprise and some by bureaus, Niskanen points out that in the nineteenth century many of what are now considered essential public services were provided by the private sector under contract. He then goes on to say:

The primary functional reason for choosing bureaus to supply these services, I suspect, is the difficulty of defining the characteristics of the services sufficiently to contract for their supply. This difficulty leads the collective organization ('sponsor' to use our earlier terminology) directly to organize the supply of these services, hoping to substitute incentives associated with loyalty to the collective organization for the motivation of profits ... The very problem which leads to the supply of some services by bureaus (the difficulty of defining output), however, creates one of the more important problems of controlling bureaus in any condition for which the objectives of the employees of bureaus are not completely consistent with those of the collective organization. The difficulty of defining the desired characteristics of a service also makes it difficult to give appropriate instructions to the bureaucrat ... When the objectives [of the collective organization and the bureau] are not consistent, the difficulty of defining output and the consequent difficulty of instructing the bureaucrat can lead to an actual output that is systematically different from that desired. (ibid., 20)

A bureau has three external relationships: with the collective organization that sponsors it and provides it with some or all of its funds; with the suppliers from which it buys factor inputs; and with its clients or customers. Niskanen emphasizes that most bureaus are wholly dependent on one sponsor and that most sponsors are wholly dependent upon one bureau to provide a particular good or service. This is what economists have come to call a bilateral monopoly relationship, characterized by threats and deference, bargaining, and appeals to common objectives.

In Niskanen's model there is a kind of exchange between sponsors and their bureaus: 'The bureau offers a promised set of activities and the expected outputs of these activities for a budget' from the sponsor. The sponsor, on the other hand, offers to 'buy' a level of promised total output for a budget. From the viewpoint of the bureau, the sponsor's demand is summarized by what Niskanen calls the 'budget-output function,' the maximum amount the sponsor is willing to pay for an expected level of output. Niskanen assumes that sponsors are willing to pay more for additional output, up to a limit, but the amount of this additional payment for additional output declines as total output increases. He emphasizes that the collective organization's demand for the bureau's output is exactly that and not necessarily the demand of the constituents of the collective organizations (voters, in the case of government).

The budget output function of the sponsor as revealed to the bureau will be related to that of the constituents through the processes by which the officers of the collective organization are selected and by its internal decision processes, but will not necessarily be identical with that of the constituents ... A bureau may appeal to the constituents of its sponsor organization in an attempt to increase the sponsor's demand for the bureau's services, but it is not the preferences of the constituents that are important to the bureau, but rather their influences on the revealed preferences of the bureau's sponsor. (ibid., 27)

Niskanen assumes that the officers of the collective organizations seek their own interests or at least want to be well regarded for their period of service. He also assumes that these payoffs to the officers are 'only weakly related to the total *net* benefits generated by the services financed by the organization' (ibid., 29).

This means that the officers have little incentive to press for efficiency within bureaus. He further assumes, at least at the outset, that the managers of bureaus have a great deal of information about the sponsor's demand for output, by having observed their past behaviour, but that sponsors know little or nothing about the costs and production processes of the bureau and therefore are in a weak bargaining position when it comes to determining bureau budgets, even if they were motivated to be tough.

Niskanen carefully distinguishes between the objective of the officers of collective organizations - re-election - and the objective of managers of bureaus - budget maximization. After reviewing alternative assumptions, Niskanen takes the position that while managers undoubtedly have a number of personal objectives (e.g. salary, perquisites of office, public reputation, power, patronage, output, ease of making changes, ease of management, etc.) all of them are strongly

and positively related to the size and rate of increase of a bureau's budget during the management's term of office. He then treats the size of the bureau's budget as an adequate proxy for the other, perhaps more high-minded, objectives of bureau managers. He believes that even though individual managers may not be anxious to maximize their budgets the pressure from their subordinates and the officers to whom they report forces them to adopt this goal. The first pressure is obvious; the second perhaps needs some elaboration. In Niskanen's words:

Both the executive and legislative officers reviewing the bureau fully expect the bureaucrat aggressively to propose more activities and higher budgets. In fact, these officers would not otherwise know how to perform their review role. They lack the time, the information, and the staff necessary to formulate new programs. They depend on the bureau to seek out and propose new programs and to make a case for larger expenditures in old programs. The total activities and budget of most bureaus are beyond comprehensive understanding, so the executive and legislative officers focus most of their review on the proposed *increments* and reveal their priorities by approving different proportions of these ... If agencies refuse to be advocates, congressmen would not only have to choose among the margins of the best programs placed before them, they would also have to discover what these good programs might be. (ibid., 40)

Three additional assumptions used in the simplest Niskanen model are important. The first is that bureau managers do not reveal to their sponsors their minimum cost conditions, so that the latter never 'really' know what it costs to produce a given level of output in the most efficient manner. The second is that managers are 'discriminating monopsonists'; if they have to pay higher prices to attract more inputs, they do not pay these higher prices to those inputs that were willing to work for less. Third, the minimum cost of producing additional units of output rises as output rises.

Using these assumptions Niskanen is able to demonstrate algebraically and geometrically that while bureaus may or may not produce inefficiently, they *always* produce too much in the sense that the value to the sponsors of the last units of output will always be less than their cost. That is to say, if sponsors cut budgets they would reduce costs more than benefits, so that the net benefits from programs would rise.

Niskanen makes a vital distinction between what he calls 'budget-constrained' and 'demand-constrained' bureaus. The former have budgets sufficiently small that even with the least-cost methods of production the last units of their output would have a positive value to the sponsor. The former have budgets sufficiently large that with least-cost methods of production the last units of their output

would have zero or negative values to their sponsors. The budget-constrained bureaus have an incentive to improve their efficiency because by so doing they can produce more output than the sponsors expect, which will probably lead to greater budgets in subsequent years. Demand-constrained bureaus, on the other hand, must somehow or other use up their budgets without producing greater output if they are not to have their budgets cut. In fact, of course, where the budgets of bureaus are controlled at the activity level, it is possible to find in a single bureau simultaneous attempts to economize in some activities and spendthrift behaviour in others. The main point that Niskanen seeks to make is that 'the main reason for concern about bureaus (in the budget-constrained region) is not efficiency at the equilibrium level of output, but the oversupply of services' (ibid., 63).

It is not possible, nor probably desirable, to try to summarize in detail all of the implications that Niskanen draws from his elaborations of this simple model. Among a host of other observations those listed below are, however, of particular interest to us.

- 'Bureaus will seek to increase the sponsors' demand for their services and reduce the elasticity of that demand (i.e. make the sponsors more insensitive to budget costs).
- 'The budget-maximizing motivation for bureaus will lead them to add to the range of services supplied and become less specialized. This is desirable because it reduces the monopoly power of other bureaus.
- 'Most public administrative reforms - which group bureaus supplying similar services into larger specialized monopoly bureaus - represent attempts to shape the bureaucracy to fit the review process. Such reforms are inherently perverse. In the short run, they increase the monopoly power of the bureaus. Over a longer period, the bureaus will again broaden their service line, and the orthodox criteria of public administration will suggest another (also perverse) reform. In contrast, a program-budgeting system represents an attempt to shape the review process to the present and evolutionary conditions in the bureaucracy' (ibid., 112).
- 'Unfortunately, for long-term investment decisions in an environment where bureaucrats have a relatively short tenure, budget maximizing behaviour appears to be uniformly ineffective' (ibid., 123).
- 'In conditions where emigration is very costly,[3] the primary reasons why the existing forms of representative government do not necessarily generate optimal behaviour are the following: 1/ The election processes generate very little information about the population's demand for specific public services ... 2/ The

3 An example of 'costly' emigration would be an elderly person fluent only in his native language, which was rarely spoken elsewhere.

elected officers of higher level governments, in most conditions, have very poor information on the minimum total cost to supply a specific service ... 3/ There is no apparent characteristic of government (such as the political analog of a stock option) that would make the motivations of the executive and legislators consistent with maximizing the total net benefits to the entire population ... 4/ There is an "invisible hand" in governmental affairs, but it is a helping hand for some, a barely acceptable appendage to many, and a mailed fist for others' (ibid., 135–7).

– 'The general effect of the majority rule selection of the output of a public service, if the service is available at an objective price and the tax price to each group is equal, is thus to benefit the high-demand group at the expense of the low-demand group ... The effect of logrolling is similar to the effect of averaging the bill at a restaurant; each person has more of an incentive to order a high-priced menu than if the bills were separate' (ibid., 143).

– 'The more disturbing fact is that good men who work very hard at their jobs, in certain institutional conditions, can and do make an awful botch of things. The important challenge is to identify those institutional conditions for which a representative proportion of rascals is tolerable and good men are more effective' (ibid., 153-4).

One of the weaknesses of Niskanen's theory is that it does not account for what, in a Canadian setting, are called the 'central agencies.' The non-elected heads of these agencies do *not* gain prestige and influence by having a larger budget. If anything, the reverse is the case: it reduces their credibility when arguing for stringency with other departments and agencies. It appears that they grow rapidly (numbers and budgets) only under two circumstances: when there are majority governments under parliamentary systems there is usually an increase of centralization; when the central agencies have lost control over 'the system' they require more bureaucrats at the centre to negotiate with the larger number at the periphery. In neither case, however, is it true that the heads of the central agencies seek larger staffs, and the budgetary increases required, for their own sake.

Albert Breton

Albert Breton's long awaited book entitled *The Economic Theory of Representative Government*[4] was released recently (1974). While the title seems to claim somewhat more, the author's stated purpose is 'to provide a theory capable of explaining the measured and observed pattern of government expenditures and taxation for the democratic countries for which data is available' (Breton, 9).

4 It perhaps should be pointed out that drafts of the present study had been prepared and circulated before Breton's work was available.

Clearly, this purpose is closely related to the objective of the present study, though it is more grandiose. Breton seeks to explain the budgetary outcome; the present study seeks only to explain the relevance of the budgetary *process* to the outcome. The objective of the present study is also narrower in that it only purports to deal with parliamentary democracies in general and Canada in particular. Breton seeks to deal with all democratic systems of government and even offers some comments on communist regimes.

It is exceedingly difficult to summarize Breton's book because, despite its brevity, it covers a great deal of ground in an extremely condensed fashion. Moreover, the arguments are closely reasoned and integrated. It is a book that needs to be studied, almost on a line-by-line basis, rather than simply read. It is therefore with trepidation that the author of this study seeks to summarize and evaluate in a few pages the essence of Breton's argument. Further examination of the book might lead to a different emphasis and understanding.

The first point to be made about Breton's book is that it attempts to integrate and elaborate upon the work of the authors discussed earlier: Downs, Buchanan, Tullock, Olson, and Niskanen, plus others who have adopted the same conceptual framework, that is, self-interest theories of collective decision-making in the public sector. While some of the following comments are critical, they should not be interpreted as a rejection of Breton's basic thesis. He has undoubtedly achieved a major advance in what we view as the most promising theoretical approach.

The second point to be made is that Breton's basic methodology is that of comparative statics. An initial equilibrium state is postulated; there is an assumed change in one of the variables; the prices and quantities that would prevail in the new state of equilibrium are then deduced. As Breton himself clearly recognizes, although this method is a powerful tool for some problems, it does not easily handle problems of lags, simultaneous changes in several variables, and strategic behaviour, which are all aspects of reality. It should be noted that Downs, for example, failed to specify whether he was analysing static or dynamic preferences.

Thirdly, the approach adopted by Breton purports to be positive (predictive) rather than normative, although, as Breton also admits, it is difficult to keep normative elements from intruding, even with the best of intentions.

Breton emphasizes at the outset a point made above that the pure theory of public expenditure rationalizes the existence of government activities but has little if anything to say about the size of the public sector or the allocation of the costs or benefits from it among individual citizens. He points out, quite rightly, that the theory of pure public goods is a 'theory devoid of any decision-making mechanism' (ibid., 4).

He introduces a definition of 'non-private goods' that is less restrictive than the usual definition of pure public goods, namely, a non-private good is one that, although not available equally to all, has the property that the amount enjoyed by one individual does not reduce that available to others *by an equal amount.*[5] This seems a useful modification when dealing with problems of collective choice in the public sector relative to the more stringent definition of pure public goods requiring that one man's enjoyment of a good not reduce that of any other. There are many instances of non-private goods but relatively few of pure public goods.

Breton has, in his second chapter, an interesting discussion of the outputs of governments. He argues that the outputs of governments are policies and that two aspects of policy must be distinguished: objectives and instruments:

At a formal level, one can define a policy objective as a variable which enters the utility function of the individual members of a government's jurisdiction, while a policy instrument is one which does not. Such a definition is useful, but mostly in pointing out that members of society will often disagree on what is an objective and what is an instrument. This disagreement is at the heart of much misunderstanding about the governmental process, for if a citizen defines a policy as an instrument while the government takes it as an objective – or vice-versa – the citizen will accuse the government of inefficiency even if by hypothesis we assume that the government acts so as to minimize the real alternative costs of achieving what it takes to be a policy objective (ibid., 17).

He then goes on to say: 'I resolve these problems by assuming that the basic objective of the governing party is the maximization of a utility function defined for a probability of re-election variable and for other variables that will be introduced later; indeed, I assume throughout that a governing party will treat a policy as an objective if doing so will increase its utility and that otherwise it will treat that policy as an instrument.'

These definitions are extremely important for Breton's analysis because his whole book is concerned with the factors that determine the demand for, and the supply of, public policies. Several questions immediately come to mind, however. One wonders if it would not be better to emphasize that there are at least four aspects to every public policy: 1/ the magnitude and allocation of the gross direct benefits of a policy (where benefit is defined in terms of the personal utilities of consumer-citizens); 2/ the magnitude and allocation of the gross direct costs of a policy (where cost is defined in terms of the personal utilities

5 Ibid., 5, n.4. This definition was first presented in Breton (1965).

forgone by consumer-citizens); 3/ the magnitude and allocation of the indirect benefits; and 4/ the magnitude and allocation of the indirect costs. In my view, the point is not that we get confused about the distinction between a policy objective and a policy instrument, as Breton claims, but that a change in a given policy instrument simultaneously affects the utilities of a multitude of individuals in diverse ways, some directly, some indirectly, some positively, some negatively, some to a great degree, and some to an infinitesimal degree. Too frequently, assessments of the efficiency of changes in policy instruments are judged without taking into account the allocation of the direct or indirect costs and benefits.

For example, maintaining a defence base in a depressed area may be a costly way of achieving a given level of national security. But it may be an efficient way of maintaining incomes in the area. It may also be an efficient means to the achievement of the politicians' purpose – electoral support. To argue that maintaining such bases is inefficient is to assert implicitly either that these indirect effects are valueless or that they could be better achieved in a less costly manner. The first is a personal value judgment; the second is a difficult factual question that cannot be simply asserted.

Still another basic question is posed by Breton's treatment of the definitional problem. He *assumes* that governing parties, as collectivities, have utility functions and that one of the main arguments (variables) in such functions is the maximization of the likelihood of their re-election. This, it seems to me, is a questionable proposition. It implicitly assumes that all of the current and prospective members of the governing party have identical and/or stable interests or have reached a stable compromise.[6] His notion of the utility function of the governing party comes close to, if it is not identical with, the concept of a social welfare function. He assumes, in effect, either that the members of the governing party are unanimous in their tastes and preferences, an unlikely event if the cabinet is representative of diverse regional, industrial, occupational, religious, and other interests, or that they have reached a permanent compromise, an unlikely event when the newspapers each day reflect changes.

Having considered a range of public policies within the framework just described, Breton turns in chapter 3 of his book to a discussion of what he calls 'The institutional framework.' The three dominant characteristics of that frame-

6 Given that the cabinet is representative of diverse regional, industrial, occupational, religious, cultural, and other interests, it would be surprising if the members were to hold a common set of tastes and preferences about policy objectives. While the notion that cabinet members negotiate a compromise is much more plausible, it is difficult to imagine a compromise that encompassed *all* of the objectives of all of the members and was stable. The relative bargaining power of ministers shifts daily, as public attitudes change and new information emerges.

work, he believes, are voting rules (he terms them decision rules), the length of the election period, and the degree of full-line supply. He argues most persuasively that in the absence of a unanimity voting rule, election periods of zero length, and a single-issue campaign platform, politicians, and political parties are shielded from the preferences and the pressures of citizens. 'The shield is not a perfect one, of course, and the extent of its efficiency depends on the level at which the various characteristics are fixed, but unless unanimity prevails, the length of the election period is zero, and preferences count for each and every public policy separately, politicians and political parties have a number of degrees of freedom at their disposal which they can use as they please' (ibid., 43). Two observations seem pertinent. Breton's list of the factors that shield politicians is obviously incomplete. The rules that determine the selection of electoral boundaries, campaign financing, and government secrecy, for example, are clearly important. Secondly, he does not seek to explain how politicians (the governing party?) are likely to try to use this latitude.

Building on the concepts previously described Breton then develops a theory of the demand for public policies. This theory involves only a small modification from the static demand analysis for private goods in traditional economic analysis: the citizen's demand for a particular public policy depends upon its own price (taxes required to pay for it), the prices of all other policies and goods and services, income, and tastes and preferences. The crucial difference between the traditional theory of the demand for private goods and the theory of the demand for non-private goods, in Breton's formulation, is that in the former instance the individual adjusts his demand, as a result of a change in one of the foregoing determinants, by buying more or less or by selling more or less. In the case of public policies, however, these kinds of adjustments are not readily made. It is difficult, if not impossible, for an individual to sell some or all of his access to a public good that he does not want; similarly it is difficult, if not impossible, for him to buy more of a public policy he desires in the usual market kind of transaction. This disparity is of crucial importance in the Breton analysis.

This concept is so important that his definition should be quoted in its entirety:

I will call the difference (whether positive or negative) between the amount desired of public policies (at existing tax prices and incomes) and that provided, the degree of coercion imposed on citizens, and I will assume that coercion is (absolutely) greater, the larger the difference between the two magnitudes ... [This definition] emphasizes the difference between the situation of a consumer who is in a state of equilibrium but is capable of engaging directly in actions that will remove the disequilibrium but unable to buy and sell and therefore only able to affect his own position by influencing politicians. (ibid., 57)

Breton's point is not that the governmental party intentionally coerces individuals in this way. Rather, he argues that when there are large groups with different incomes and tastes, and non-private goods are being provided by the state, it is virtually impossible to provide each citizen with what he wants in the way of these goods at any given set of tax prices. The problem of coercion arises because public goods are necessarily consumed by groups, and the taxes imposed on the individual members of the group cannot reflect how much each member desires them.

Without going into the matter in too great detail, there seem to be several difficulties in this approach. First, it is assumed that, when the individual is provided with non-private goods that he values as highly as the private goods forgone to obtain them (the tax price), no coercion exists. It is further assumed, as a kind of corollary, that when coercion does not exist, as thus defined, the individual will not attempt to alter public policies – whatever the potential benefit relative to the potential cost to the individual. This seems a rather peculiar notion. Let us suppose that no coercion exists, as Breton defines the term. Why would an individual not seek to change policies through influencing politicians if he believed that the potential benefits (increased benefits or reduced costs) exceeded the probable costs involved in exerting the influence? The idea that no coercion equals no political action seems to play the same part in Breton's theory that Pareto optimality plays in welfare economics. Neither admits of the possibility that A is quite willing to gain at the expense of B if the potential payoff is sufficiently large relative to the investment of time and effort required to obtain it.

Secondly, Breton's formal presentation seems to suggest that the individual is faced with a given change in the quantity and quality of a public policy. His demand for it is therefore a function of its tax price (the additional tax required) and the individual's income and tastes. The degree of coercion is thus determined by the change in the tax imposed on the individual to 'pay for' the policy (ibid., 57–66). He further assumes that governing parties have no knowledge of the preferences of citizens when introducing change in either the pattern or quantity of public policies (expenditures or taxation) (ibid., 57). In fact, are these decisions to offer policies and to impose taxes reached sequentially, as Breton assumes, or simultaneously? Does the governing party have *no* information about the desires of the electorate before 'initial' decisions are made?

Thirdly, as Breton freely admits (ibid., 67), when the changes in taxes imposed on individuals are used to finance a whole bundle of changes in public policies, it is impossible to isolate the incremental tax cost associated with any particular policy change. It follows, in Breton's view, that the individual therefore relates his feeling of coercion to the feeling of 'fair' and 'unfair' taxation he experiences when contemplating the policies he gets. He does not relate 'fairness' to the traditional dimensions of equity: 'Am I paying too much tax relative to

people who are essentially in the same circumstances (horizontal equity)? Am I paying a tax that is appropriately different from those in essentially different circumstances (vertical equity)?' It all seems to come down to the idea that those who feel cheated take political action. But what of the people who would like to cheat others? Would they not be willing to take political action if the price of cheating were right, relative to the possible gains?

Fourthly, for the present purpose, perhaps the greatest limitation of Breton's analysis of the causes of political activity is that it is non-operational. Who is to say when a man will feel so unjustly treated that he will be willing to take political action? The concept of coercion rests entirely on subjective factors. Those who, in the event, take political action are coerced – by definition.

Breton considers in his fifth and sixth chapters how citizens, 'motivated by their own self interest, can seek to achieve partial or complete elimination of the coercion (or of the expected coercion) imposed on them by the governing party and in the process signal or reveal their (positive or negative) preferences for public policies' (ibid., 74). The principal techniques he distinguishes are large pressure group activities, individual and small group activities, social movements, individual economic adjustment, private provision, interjurisdictional mobility, and voting. He argues that when the degree of coercion experienced by an individual exceeds some positive threshold, and/or the individual perceives that others are likely to be successful in political activities that might increase the degree of coercion he will experience in the future, one or all of these retaliatory or defensive actions are likely to be undertaken.

Without wishing to denigrate the many valuable insights contained in these chapters, what seems to be missing is a notion of relevance of the costs of political participation relative to expected benefits. Surely the individual makes a decision to engage in political action, and chooses the particular form of that action, on the basis of the expected rate of return on his investment of time and money in achieving or preventing changes in public policies. Even if the individual is not being, and does not expect to be, coerced in Breton's sense, it will be sensible for him to engage in political action if he thinks he can get at least a normal return on his investment. Clearly this could involve obtaining a tax reduction, or an increase in benefits that exceeded the additional tax cost (if any).

In short, what Breton seems to ignore is the possibility that individuals, following their self-interest, are prepared to use the state as an instrument to coerce other individuals if this were to their advantage. Moreover, although he does mention the importance the individual voter places on the expected behaviour of others, he does not seem to accord adequate weight to strategic questions. In calculating the likely payoff from political activities, estimates of the retaliatory activities of others are of crucial importance.

In the third part of his book Breton turns from an analysis of the demand for public policies to a detailed discussion of the factors that determine their supply. This involves, in particular, the consideration of the behaviour of political parties and bureaucracies.

Of crucial importance in Breton's analysis is the assumption that individual politicians seek to maximize their own utility. This is determined, according to him, by 'personal pecuniary gains, personal power, his own image in history, the pursuit of lofty ideals, his personal view of the common good, and others which are peculiar to each politician' (ibid., 124). Because these sources of the personal utility of the politician are only available to those who hold office, according to Breton, we can assume that a politician will adopt policies that maximize the likelihood of re-election.

In his view, politicians who are members of the governing party trade with one another, through various kinds of logrolling, until a stable coalition is obtained. The coalition then shares a common utility function in which the probability of re-election of the group is a dominant, if not the sole, variable that influences policy decisions.

This method of moving from individual utility functions to a collective utility function is certainly ingenious. It is clearly superior to the approach which assumes that all members of the governing party share the same tastes and preferences – the Downs assumption. But one cannot help wondering whether it is necessary to introduce the notion of a collective welfare function for the governing party. There seems little doubt that the members of the governing party do not have identical tastes and preferences (interests) and that they reach a series of rolling compromises among their conflicting interests. It is true too that the nature of the compromises is not independent of such factors as the length of the election period and the voting rules. What is difficult to accept is the whole concept of a collective utility function for a group of individuals who are as much competitors as they are colleagues. Usually, all members of the ministry can agree that obtaining re-election is 'a good thing.' But it is not difficult to conceive of circumstances where a contender for the leadership has much to gain from the defeat of the governing party at the polls. It opens up the leadership! There are other examples too.

Would one not come to the same conclusion by dropping the concept of a utility function for the governing party? Why not simply assume that the probability of re-election (or of being a member of the party forming the government) is an important factor in the utility function of each politician, just as the probability of continuing to hold a job is important to most members of the labour force. That the members of the governing party coalesce to make a package platform can hardly be denied. Whether they are equally and jointly committed to re-election is another matter!

In short, on what grounds can one assume that there is a consistent ordering of policy preferences by ministers? That they engage in trades among policies seems clear; that they come to some kind of a reconciliation in most circumstances is also indisputable. That they end up assigning the same weight to the re-election of the party, as distinct from themselves as individuals, is something else again. Every time a minister makes a speech or grants an interview he is trying to turn the terms of trade in his favour.

Breton recognizes this in his discussions of party strategic behaviour where he points out, particularly in section 2 of chapter 7, that voters have imperfect memories, with the result that politicians in the governing party can exercise their power much more effectively in the first few years after their election than they can just prior to the next election.

In chapter 8 Breton analyses the 'technical constraints on the behaviour of the governing party.' He states:

The fact that the extent of coercion to which one citizen is subjected depends, in part, on the extent of coercion imposed on other citizens, is, from the point of view of the governing party, a technical constraint to which that party must respond and adjust. To do so it can engage in one or more of four basic activities; it can (1) enact and implement discriminatory activities as well as policies that have the characteristics of pure private goods, including changes in tax rates, basic exemptions, tax credits, loopholes, etc.; (2) discriminatorily adjust the penalties levied against or the probability of apprehending those committing legal offenses; (3) engage in implicit log-rolling, combined with full line supply by combining policies in such a way as to elicit or maintain political support; and (4) seek to alter the preferences of citizens so as to reduce the differences that exist between them and thus make them more homogeneous. (ibid., 143)

In analysing each of the strategies Breton assumes that the governing party seeks to reduce the degree of coercion. What he does not seem to accept is that the governing party is required, not to reduce the degree of coercion per se, but to be perceived to be the least repugnant alternative party to the marginal voters in marginal ridings. The governing party need not eliminate coercion, as Breton defines the term. It must only *appear* to be the party least likely to coerce them in the future, or most likely to give them a net gain.

'The behaviour of bureaus' is discussed by Breton in chapter 9. Breton accepts Niskanen's assumption that bureaus seek to maximize the size of their budgets. Given that the policy decisions of politicians are 'influenced, and sometimes largely shaped by bureaucrats' (ibid., 161), the objectives of the latter are of great importance in examining the policy decisions of the former.

Breton defines size as either the number of employees of the bureau or the relative size of the government's total budget devoted to programs administered by the bureau. He argues that 'it is through maximization of this objective that bureaucrats are able to achieve the highest possible income and prestige consistent with the constraints to which they are subjected ... It also implies that bureaucrats are not responsive to the preferences of citizens, but are solely guided in their actions by the network of relationships linking them to politicians and other bureaucrats' (ibid., 162). He continues: 'The fact that the behaviour of bureaucrats is to some extent determined by interaction with politicians implies, of course, some indirect response to the preferences of citizens, since politicians are given the institutional framework responsive to these preferences; but except for this relationship bureaucrats have a professional life of their own and a pattern of life unrelated to the preferences of citizens' (ibid.).

The result, according to Breton, is that bureaucrats overestimate the benefits and underestimate the costs in order to make large projects look more attractive; they support policies that require complicated administrative machinery; they advocate the revision of old legislation rather than its abandonment; they prefer programs that offer benefits in kind rather than in money; they like economic planning rather than the operation of free markets.

The major technique used by bureaucrats to accomplish these results, according to Breton, is the manipulation of information flows through the bureaucratic hierarchy. In Breton's view, senior bureaucrats are forced to bribe their subordinates in order to obtain the information they require. The larger the base of the bureaucratic pyramid, and the higher its apex relative to the base, he believes, the larger the total bribes must be. Furthermore, Breton states, many of the features of bureaucratic structure are designed to reduce the bargaining power of the bureaucrat and hence the size of the bribe that must be paid to obtain the requisite information. He also makes the point that most bureaucratic structures are successful in reducing the power of bureaucrats to bargain over the release of information, so that the strategic behaviour by bureaucrats is generally of little importance. He concludes that it is usually possible to ignore the role of strategic behaviour within bureaucracies without 'analytic loss' (ibid., 168).

Several questions might be raised about Breton's analysis of bureaucratic behaviour. First, although the idea that bureaus seek to maximize their budgets (or employment) seems a plausible hypothesis for operating bureaus, it is doubtful that this explains the behaviour of the most important bureaucrats, as discussed above. To use the titles employed in the Government of Canada, it is highly doubtful that the secretary of the cabinet, the deputy minister of finance, the secretary of the Treasury Board, and the chairman of the Public Service Commission seek to maximize their budgets or employment. Second, that bureaucrats

are not particularly sensitive to the desires of citizens *in general* is probably true. But a deputy minister with strong support from a pressure group has more bargaining power. Third, the view that control over information flows confers power (influence) in a bureaucracy is beyond dispute. But the notion that senior bureaucrats are forced to bribe their subordinates to obtain information seems extreme. Senior bureaucrats have control over the promotions of their subordinates. When superiors are embarassed by their subordinates because information has been withheld the result is likely to be the withholding of advancement. The possibility of the stick is more likely to be persuasive than that of the carrot. Fourth, it is strange that Breton claims that many features of bureaucratic structures are designed to reduce the bargaining power of bureaucrats while at the same time arguing that the strategic behaviour of bureaucrats, particularly with respect to the control of information flows, is of little importance. Finally, Breton seems to give inadequate attention to the fact that, for ultimate decision-makers (in this case ministers), the binding constraint is time. Some method of condensing and screening the flow of information to reduce its volume is inescapable. The important question is not whether condensation and screening occur but the basis on which it is done.

In the third section of chapter 9, Breton considers the empirical work done by Davis, Dempster and Wildovsky (ibid., 169) concerned with estimating the changes in government expenditures over time in the United States. The problem with the DDW equations, Breton acknowledges, is that they do not explain the shift points – discontinuities in the rates of growth of expenditures on particular programs. This is equivalent to a theory of the business cycle that does not explain turning points! Given that a parliamentary system (and probably any other democratic system for that matter) can only cope with a limited number of basic policy changes in any year, it follows that the budgets of most existing programs will appear to grow on a pro-rata basis. But a few shift points per year can produce a massive re-orientation of the public sector in a decade!

The whole notion of incrementation or marginalism is suspect, as discussed below. The decision to adopt a new program (e.g. medicare) or revise an existing program (e.g. unemployment insurance) may have a marginal impact on expenditures in the first year but have a massive impact on the budget over time. To claim that the change in the first year was incremental, because it was small relative to the total *in that year*, is to miss the point.

Breton has two possible explanations of the constancy of the rate of growth of expenditures on particular programs: the constancy of the bargaining power of the parties, both political and bureaucratic; the costs of bargaining may be so high that the parties adopt rules of thumb. That is to say: ‘changes that lead to variations in the position of bureaus are conductive to strife and to the disrup-

tion of the internal organizational rules of the institution and as a result will be engaged in as seldom as possible'. (ibid., 173). This may go some way in explaining 'incrementalism.' It does nothing, of course, to explain the shift points that are so decisive in accounting for the changes in the size and composition of the public sector.

In concluding chapter 9, Breton argues that, on the supply side of the public sector, 'the dominant force in shaping the pattern of expenditive policies and tax-prices is the relative power of politicians and bureaucrats (ibid., 175). This is a strong conclusion, given the argument that preceded it.

The last section of Breton's book, entitled 'Resource allocation in the public sector,' in three chapters puts his theory through its paces, as all comparative static theories must be tested. The demand for public policies is dependent on three factors, in Breton's view, as explained in chapter 10: 'the preferences of citizens for public policies, as these are related to the incomes of citizens, and to the tax-prices that have to be paid for these policies as well as the costs of using the instruments of political participation' (ibid., 179). On the supply side, Breton also distinguishes three factors: the degree of competition faced by the governing party created by opposition parties, the degree of interest which this competition stimulates in the electorate, and the relative bargaining strength of politicians and bureaucrats that 'determine the instruments used by politicians in order to reduce the degree of coercion ... and the policies that will be implemented' (ibid.).

Although the argument is not entirely clear, at least to me, Breton's point seems to be that when the costs of political participation are low (that is to say, citizens can let the governing party know which policies in that party's platform they want at low cost relative to the benefits they hope to obtain), the governing party will be faced with a large number of alternative policy packages. All of them will be successful in electoral terms. On the other hand, when the costs of political participation are high, the governing party will be unaware of the desires of others, at least relative to the support required for re-election. In the first instance - low participation costs - politicians have more room to manœuvre; in the second instance - high participation costs - the governing party has little space. Indeed, in the extreme case the governing party does not know enough about citizen's preferences to put together a platform that will result in its re-election.

As we understand it, Breton's view is that the choice of the mix of policies is determined by the relative bargaining power between politicians of the governing party and the bureaucracy. When the costs of political participation are low, the range of alternatives is larger, and therefore the likelihood of reaching a political-bureaucratic compromise consistent with the re-election of the govern-

ing party is greater. The converse also holds, in Breton's opinion. When participation costs are high, the range of feasible options is low, and if the bargaining power of the bureaucracy is relatively great the governing party may be forced to adopt a policy bundle that will result in its defeat.

Several questions come to mind. Breton seems to assume that knowledge of the policy preferences of an adequate number (or proportion) of voters guarantees electoral success. But what if their preferences are inconsistent, so that pleasing any one group displeases others who have, collectively, the balance of power? Another point is that Breton does not really explain the source of the bargaining power of bureaucrats, which is crucial in his model. That bureaucrats have influence is fully accepted: that bureaucrats have enough *power* to force the governing party to accept knowingly a losing policy package is by no means obvious. Why not send one or two recalcitrant bureaucrats off to innocuous postings to encourage the others? Behind every senior bureaucrat are a number of hungry aspirants, both within and outside the service, who often have a great deal of the information that politicians want.

Breton tries to escape from this problem by assuming that every voter will support the governing party if he or she is not coerced. But, as argued earlier, voter A may not support the governing party if he perceives that it is likely to increase the degree of coercion imposed on voter B (an enemy) or to reduce the coercion imposed on voter C (a friend). Moreover, even if voter A approves of the promised actions of the governing party, what if he perceives that the opposition party (or a coalition of such parties) is more both likely to be elected *and* more likely to do even more if elected?

Leaving aside his interesting analysis of two case studies, chapter 11 concludes with a section on 'the empirical analysis of government policies.' In essence, what Breton seems to be saying is that government expenditures are a function of eight factors (ignoring random components): 1/ the power of bureaucrats relative to that of politicians in the governing party, 2/ the tax-prices associated with alternative expenditure policies (as distinct from policies that do not require public expenditures), 3/ the money incomes of citizens, 4/ the political participation costs of citizens, 5/ changes in the mix of policies involving tax costs rather than economic (private) costs (e.g. regulations), 6/ the poor memories of citizens, 7/ the degree of competition among political parties, and 8/ the rates of discount applied to future costs and benefits by citizens and politicians.

In his concluding chapter Breton emphasizes that his contribution has been to take into account two fundamental ideas: the means by which politicians gain degrees of freedom through long election periods, non-unanimity decision rules, and full line supply; and the importance of public (and non-private) goods. In his view, it is the partial substitution of these ideas for Downs's virtually exclusive

concern with information costs, plus his incorporation of the role of the bureaucracy, that are particularly important. These are, indeed, major advances.

PROGRAM PLANNING AND BUDGETING

In recent years Program Planning and Budgeting (PPB) has swept through the fiscal world like wildfire. Like most 'big ideas' the terms mean different things to different people and are supported or rejected for a whole range of reasons. Unlike the vague general theories considered so far, at least some aspects of PPB are concrete and pragmatic. It is the stuff that practical men can readily grasp and implement. But like the rarefied atmosphere of the theory of pure public goods, social welfare functions, and interest groups, the harder one presses the concept of PPB the more elusive it becomes. On reflection this is hardly surprising, because ultimately we find ourselves faced with the same intractable problems. Only the answers differ.

It is generally accepted that PPB has three related purposes: the classification of government activities in terms of goals and objectives (taxonomic purpose); the comparison of costs with outcomes and the consideration of alternative means to achieving the same outcomes (analytic purpose); and the long-range planning of government programs (projective purpose). The following sections deal with each of these purposes in turn.

The taxonomic purpose

This purpose is apparently straightforward. In earlier years the *Estimates* and the *Public Accounts* (the first being the government's expenditure proposals on which the legislature votes and the latter being a statement of what was actually spent relative to what was actually voted) were designed primarily to achieve accountability and management control. It was assumed that most government outputs could not be measured, at least in an objective manner. It was also assumed that no global measure of effectiveness, such as the rate-of-return calculation of the private sector, was available for government activities. Therefore, the legislature, by long-standing tradition, insisted on controlling expenditures on inputs on a line-by-line basis (one line for every object of expenditure such as wages and salaries) for each responsibility centre (identifiable organizational unit reporting to a designated minister). This was satisfactory, as far as it went, and the same kind of information is required today for the same purpose. At least three difficulties arose, however. Line-by-line budgeting tends to draw the attention of legislators away from the big issues and towards the minutiae of travelling expenses, office furniture, salary scales, and so on, which everyone believes he understands. Secondly, it was often difficult to discover how much was being

spent in total on particular functions (e.g. education) because many organizational units carried out some educational functions. Thirdly, the ostensible purposes of some expenditures were often difficult to determine from the vote wording, so that legislators were often ill-informed about the purposes for which the dollars being voted were actually going to be used.

The classification of expenditures by activities (and bundles of related activities designated as programs), each with its own descriptions and stated purpose, was intended to solve these difficulties. In most jurisdictions that have adopted PPB some progress has been made in realizing this taxonomic purpose. In none has success been complete. In many jurisdictions, PPB is in reality nothing more than a few shaky steps along this taxonomic road. Among the difficulties encountered in proceeding to do what seems like a simple exercise, the following points are particularly worthy of attention.

Programs are composed of one or more activities. Each activity is made up, usually, of a number of subactivities, and subactivities consist of groups of sub-subactivities in an almost infinite regression. How much disaggregation is the right amount? For that matter, why not designate each activity as a separate program and let the subactivities be termed activities? It is obviously possible to contract or to expand the number of programs almost at will.

Many government activities produce intermediate outputs that are inputs into a number of programs carried out by more than one department. How should these costs be allocated? How can responsibility accounting be maintained at the same time without complex and confusing reconciliation statements?

Perhaps the most serious difficulty, however, arises in the attempt to define program goals and objectives. As we have discussed elsewhere at length, there is often serious controversy generated in the attempt to define program goals. Ministers want to express goals in terms that are likely to persuade the public of the government's good intentions and positive approach to the resolution of problems. Many ministers, and virtually all bureaucrats, seek to define goals in such a way as at least to defend, and preferably to expand, their existing jurisdiction. In principle there is no problem a government can face that is not the responsibility of some minister. While some responsibilities are assigned clearly and unequivocally (often by statute), there are usually many grey jurisdictional areas where interministerial and/or interagency warfare is being waged, at least in a quiet way. Requiring departments to define their program objectives frequently brings these conflicts into the open. It may induce wording designed to 'give nothing away' or provide a beachhead for a later assault. The analyst has his own purposes in trying to influence the definitions of program objectives. Ministers and most bureaucrats have a strong incentive to define objectives vaguely and rhetorically. The analyst responsible for assessing the effectiveness of programs

has exactly the opposite motivation. He wants clear, precise, and measurable objectives. He also wants his superiors to define the objectives, because, after all, the lowly technician cannot advise the government as to its purposes. He also wants someone to think through the purposes behind the purposes: the purpose of this program is to educate children. But what is the purpose of educating children? To raise their incomes. But what is the purpose of raising their incomes? To improve their standard of living. But is this not the purpose of dozens of programs? Ad infinitum.

Still another difficulty arises in distinguishing between stated purposes and unstated and/or unintended effects. While the stated purpose may be x, it may have effects, favourable or unfavourable, on other objectives. Presumably, unfavourable side effects should not be publicly acknowledged. But perhaps favourable side effects should be elevated to the status of additional program objectives to strengthen the case for the program. But this may raise, in an intense form, some of the jurisdictional conflicts mentioned before.

This question of the definition of objectives is not, unfortunately, just a silly semantic game, although undoubtedly that is often how it is treated. It is *not* simply a matter of getting a few intelligent men of goodwill to sit down and 'sort it all out' in a few days or weeks. Leaving aside the political significance of the problem for the moment, it is by no means obvious that the task of developing a comprehensive set of operationally defined (measurable) goals is feasible if one insists that the set should be not only comprehensive but also generally accepted.

One can imagine one or two individuals completing the task, if not to their own satisfaction at least to the point where some degree of personal commitment might be achieved. It is difficult to imagine, however, a general consensus emerging among ministers except, possibly, after endless discussions and negotiating behind closed doors and provided that the results were to remain secret. It is virtually impossible to imagine a cabinet releasing, as a statement of government policy, such a set of program objective definitions.

For the reasons advanced by Downs, governments adopt programs to obtain votes. For a government to define precisely and operationally such terms as health, poverty, law and order, and so on would be to court disaster. Consider, for example, the question of poverty. Many programs seek, ostensibly at least, to reduce or eliminate poverty. But to define poverty in objective terms almost certainly would leave a government open either to the charge that it had set too low a standard ('everyone knows that a family of four cannot survive in dignity on x dollars per year') or to the charge that it had set too high a standard and that trying to 'solve' the problem would bankrupt the government and the more affluent voters and reduce the incentive to work. What proportion of the electorate

would accept any precise definition as 'just about right?' Furthermore, precise, measurable objectives would raise questions about the government's expectations concerning the degree of realization at specific target dates and, what is even more frightening, make it possible to check, after the event, on the extent to which these expectations were fulfilled. And if not, why not.

Another important point to be made about statements of government objectives is that, because most programs have multiple effects that concern ministers, what is needed is not the objective of a single program but a statement of all the government objectives that the program may affect positively or negatively. The task of the analyst is to estimate what all of those effects might be. For it is important to realize that because programs can have negative effects on objectives, a failure to spell out all of a government's objectives is tantamount to a failure to specify all of the constraints within which programs must be designed and operated.

For example, suppose that a government in order to encourage tourism operates a number of fish hatcheries designed to produce the fingerlings needed to stock lakes. If the objective of the hatchery program is defined in terms of the least-cost production of fingerlings it might well turn out that many hatcheries could be closed and production consolidated in one large hatchery located in a prosperous area without causing significant unemployment. However, this might turn a number of workers in the existing hatcheries out of their jobs. If these existing hatcheries were located in depressed areas, this unemployment might be protracted. With a fixed budget, and greater efficiency in the production of fingerlings through consolidation, more fingerlings could be produced and the incomes of tourist operators increased – but at the expense of lower incomes for the hatchery workers laid off. This may or may not constitute a net benefit. One thing is certain: ministers will not be indifferent to the layoffs and may rightly insist that those considering the hatchery program accept as a constraint that there be no layoffs of existing hatchery personnel. Ministers have, in other words, an unstated objective about civil service layoffs that, while perhaps not explicit, is certainly 'real' in any evaluation of the hatchery program.

It is important to note that, from the point of view being put forward here, the development of an all-inclusive set of operationally defined government objectives is equivalent to the specification of the arguments (variables) in a social welfare function of the kind discussed earlier. All that would be missing would be the assignment of weights to those variables in order to have the complete specification of the kind of social welfare function that some economists assume to exist.

The analytical purpose

In principle, PPB encompasses the analysis of the effects of changes in the existing and potential policy constraints of a government (including expenditure pro-

grams) on the simultaneous realization of all of its objectives over time. In principle, too, the changes in policy constraints should be considered not only one at a time but also in terms of alternative packages of changes, because some instruments are complementary while others are substitutes for one another. Since the range of possible changes in the policy instruments is infinite, the possible permutations and combinations of these instrumental changes is also infinite. The perfect analysis therefore is unattainable. Nor is this the end of the difficulty. Assume that one defines the analytic task in the narrowest possible way: what were the effects of the adoption of this particular program on the attainment of a particular government objective? Even finding that the degree of goal attainment declined is no proof that the program was ineffective. In order to show that the program was ineffective it would be necessary to 'prove' that the degree of goal attainment would have been worse without the program. This involves being able to forecast, on a reliable basis, the degree of goal attainment in the absence of the change. This, in turn, implies a great deal of knowledge about the way in which the economic or social system functions, knowledge that is usually most imperfect. It is not difficult for a strong defender of a program to argue that the forecasts of goal attainment are unreliable, or the data on which it is based were biased or incomplete, or the methodology was unsatisfactory, or the results were misinterpreted. The list of arguments is almost endless.

These difficulties are all compounded, of course, when government objectives are not specified in operational terms. Is an increase in life expectancy, as a result of improved access to health services and facilities, a good proxy measure of the improvement in the nation's health? Or should one consider, somehow or other, the quality as well as the duration of life? How? Presumably there is a set of proxy statistical indicators of the state of a nation's health. What does it mean when conflicting trends are found among the indicators included in the set?

It would take us too far afield to try to describe and evaluate all the analytic techniques that may be used to assess the effectiveness of government programs. Aside from benefit/cost analysis, which is the received method of handling this particular type of problem, any of a wide range of methods used in applied economics have been used with greater or lesser degrees of success (the degree of success being, of course, a matter of judgment). This ambiguity about the appropriate technique means that the credibility of the analyst is an inescapable ingredient in any assessment of his assessment.

Perhaps a few words should be said about benefit/cost analysis and operational performance measurement. The former method is, fundamentally, an extension of the rate-of-return calculation employed almost universally in the private sector. It compares the discounted value of a stream of future benefits (revenues in the private sector), measured in money terms, against the discounted value of a stream of costs that must be incurred to obtain those benefits where

the costs too are measured in money terms. The same calculations might be made by a firm contemplating two machines that produce the same product, one having, say, a higher initial cost and lower operating costs, the other having a lower initial cost and higher operating costs. The difference between private sector and public sector calculations is that the firm will ignore costs and benefits that do not affect it directly. It is concerned only with its own private costs and benefits. The public sector calculations encompass, at least in theory, the benefits and costs to society. This almost invariably means that the analyst has to impute the dollar values of benefits and costs for which market prices do not exist, because the whole approach requires the comparison of benefits and costs measured on a commensurate basis – dollars. But even if the logic of the analysis is valid (somehow defined), there can be wide differences of informed opinion about the imputed values. By manipulating these imputed values it is frequently possible to manipulate the benefit/cost ratio within wide limits. Yet, in the absence of market data, it is almost impossible to 'prove' that the imputed values are unreasonable. The range of legitimate disagreement between honest and technically competent individuals is so wide as to yield results that may be little better than informed judgments made without the discipline of the analysis.

Four other serious limitations of benefit/cost analysis should be mentioned. First, it is assumed that the project being assessed is so insignificant that its adoption would not alter relative prices. Second, it is assumed that all resources are fully employed, so that the market prices reflect opportunity costs (alternatives forgone). Third, the technique does not take into account the distribution of costs and benefits – a matter dear to the heart of ministers. A project that has a payoff of five to one looks the same in benefit/cost terms whether or not the one is paid by a pauper and the five are received by a king, or vice versa. Fourth, unless it is possible to array, at one point in time, a number of competing projects in terms of their benefit/cost ratios, it is difficult to interpret them.

Operational Performance Measurement (OPM), a much simpler analytic technique, has been receiving a good deal of attention in recent years. Its very simplicity means that it is easier to explain and interpret and less subject to the arbitrary judgment of the analyst.

Many government activities are routine in nature. A large volume of tangible goods and services are produced that are relatively homogeneous: mail is delivered, cheques are printed, records are kept, tax forms are processed, and so on. These outputs are almost always means to ends, which are in turn means to higher ends. Thus, subsidized mail deliveries are a means to reducing communication costs for certain users, which are a means to increased business profits, which are a means to something else even more grandiose and vague. OPM does not ask whether subsidized mail deliveries are the most effective means to those

ultimate ends. Rather, it seeks to answer a much more limited question: given that the government is going to deliver mail, for whatever reason, what is happening over time to the unit costs of mail delivery, taking into account the quality of the service, changes in the prices of factor inputs, and changes in the mix of factor inputs? That is to say, OPM is concerned with operational efficiency rather than with program effectiveness.

With the kind of operational efficiency data available it is possible to assess the rate at which factor productivity is improving. On the basis of forecasts of required outputs in the future and estimates of the rate of productivity improvement that can be reasonably expected, it is also possible to develop forecasts of input requirements. The technique does not, in and of itself, provide any information about the rate at which productivity should or could be improved, in part because it gives no information about the degree of inefficiency that existed in the base period from which the year-to-year changes are measured. This can only be ascertained by comparing unit costs for similar activities within the public sector or between the public and private sectors or by interdepartmental organization and methods studies.

The projective purpose

The third and final purpose of PPB is to assist in the planning of government programs. Ideally, the process would work as follows. Analysts would, first of all, provide projections of the values of the proxy indicators of the degree of realization of the governments objectives, given no policy changes. Ministers would then establish target values of the proxy indicators over the planning period. Analysts would next try to assemble a package of changes in the policy instruments, including changes in expenditure programs, that would most fully realize the targets. This would be done on the basis of the information obtained as a result of analyses of the effects of changes in the policy instruments in the past. More than likely this first attempt would disclose that the ministers' targets were unrealizable, in the sense of being inconsistent, for it probably would be found that there was no combination of changes that did not leave one or more targets unrealized. Ministers would then be asked to reconsider their targets, adjusting at least one downward. This new set of targets would go back to the analysts. The process would be repeated until a consistent set of targets was found on the basis of existing knowledge of what various groups of policy changes could accomplish. The set of changes consistent with the final targets would then be implemented through the development of operational plans that phased in the changes over the planning period.

This iterative procedure would be repeated at regular intervals in order to adjust for unexpected external developments (e.g. acts of God) that would alter the

realizations of the targets, changes in ministerial priorities, and greater or lesser than expected success from the policy moves.

Just to describe the planning process in this idealized fashion is to discredit it. Without the operationally defined objectives, without a reliable method of forecasting the values of the proxy variables in the absence of policy changes, given a most incomplete understanding of the effects of policy changes on the proxy indicators, it would be ludicrous to suggest that any government attempt such a procedure, even if ministers were willing to proceed in this way. For it must not be forgotten that, in effect, this type of planning would require ministers to define a whole series of social welfare functions on a trial and error basis. Each time they adjusted the target values of the proxy variables they would have consciously and explicitly to reach a new compromise among themselves, a new resolution of the conflicting interests they represent. One wonders if this approach would not make it virtually impossible for them to reach an agreement unless they were remarkably like-minded. They would be unable to play the strategic games possible in a world of greater uncertainty, where they can pretend, to one another if not to themselves, that proposed policy changes are likely to have different effects than they will have in fact.

The catalogue of difficulties could be expanded almost indefinitely, but four more will suffice for now. Politicians inevitably have to pay certain debts to those who have helped them or to provide favours that can be drawn against when future help is required. How do these kinds of decisions fit into a system that only deals with the biggest of the 'big issues' at an extremely high level of generality and abstraction?

Politicians are concerned with the public's perceptions of the government's success as much as or more than with the realities of what the government is achieving. Because many of the policies are thought to affect highly intangible things, such as 'equity,' 'community,' or 'equality of opportunity,' is it likely that the analysts will know as much as their masters in assessing the effects of policy changes on the public's perceptions? Often it is a government's show of concern with a problem, as much as concrete results, that count.

A third difficulty would arise in overloading the system. How many policy changes can a system digest in a given period of time? Public servants have to be redirected; debates have to take place and votes held; interested parties have to be consulted and allowed to have their say. The government's policy changes have to be disseminated and explained. All of this takes time and energy. Changes that come too frequently make a government appear confused and inconsistent.

Finally, but not of less importance, is the fact that the full-blown planning system described would make ministers the captives of their advisors. They would either be forced to argue with their advisors endlessly about the 'true'

effects of existing or prospective programs (where the evidence was highly technical or vague) or they would be put into the position of accepting at face value bureaucratic assessments that, if incorrect, could lead to their defeat.

It could be argued that the description of PPB just outlined is so extreme as to be a caricature of the systems either being advocated by adherents or being implemented by governments all over the world. There is considerable merit in this argument. It is undoubtedly true that what has been presented is the logical extension of the PPB concept, not the usual formulation (although the word 'usual' has not much meaning because there are so many versions) (Hartle, 1973). To help restore the balance it may be helpful to summarize briefly the views of Charles L. Schultze, director of the budget under President Johnson at the time when PPB was adopted by that administration for the civilian departments of the US government. Schultze is probably the most persuasive PPB advocate because he has modest goals for PPB.

According to Schultze (1968) PPB has six purposes: 1/ careful identification and examinations of goals and objectives; 2/ analysis of the output of a given program in terms of its objectives; 3/ measurement of total program costs for several years ahead, particularly in order to estimate the future commitments implicit in current decisions; 4/ relating annual budget allocations to longer-term plans formulated in terms of specific objectives; 5/ analysis of alternatives to find the most effective means of reaching basic program objectives; and 6/ establishment of analytic procedures as a systematic part of budget review.

In order to realize these undoubtedly laudable objectives, he proposed, and the administration adopted, certain forms and procedures. Without going into painful detail, this involved a program classification scheme, which 'should be changed as analytic need dictates' and which emphasized that programs have an output and 'should be analyzed and evaluated on the basis of how effectively and efficiently that output meets program objectives' (ibid., 25); a five-year tabular plan for each program showing, in both physical and financial terms and grouped by output-oriented categories, the impact of the current year's proposals over the period (this would be in addition to the program budget, which requests the same funds classified by objects of expenditure on which the appropriations of Congress are based); a Program Memorandum providing the 'strategic and analytic justification' for the program proposals; and Special Issue Studies, which, by mutual agreement between the Bureau of the Budget and the particular agency, would provide in-depth analytic studies of special issues. The most striking features of these proposals is their modesty. The approach is flexible and improvised, with three exceptions: relating inputs to physical outputs and to program objectives, providing information on future commitments implicit

in current proposals, and providing some analysis of the relative effectiveness of alternative proposals.

We will return to Schultze and consider his defence of PPB after a brief review of the views of what have come to be known as the 'pragmatic incrementalists.'

PRAGMATIC INCREMENTALISM

The two authors most closely associated with this approach are Charles E. Lindblom and Aaron Wildavsky. The former is concerned with policy-making as a whole, the latter with budgeting.

Lindblom

In Lindblom's (1968) opinion, individuals are incapable of producing conclusive analyses of the merits of alternative policies, both because of disputes over the goals or values that men seek through public policies and because voters and politicians do not trust analysts and analyses. They are thought of as technically incompetent, uninformed about reality, subject to unconscious biases, and/or simply self-serving.

The task and responsibility of policy-making is necessarily never assigned exclusively to one man or a small group. Even in totalitarian regimes, policy-making is a function carried out within an elaborate structure that ensures many organizations and individuals play some, albeit subordinate, part. In democratic governments the extent and depth of the involvement in the process of policy-making is, of course, much greater, encompassing ministers, officials, members of the legislature and judiciary, political parties, other voluntary associations of all modes and complexions, and the electorate. There is, in other words, an elaborate division of rights and responsibilities. Some individuals grasp the responsibilities, presumably for the income, prestige, and pride they confer. Others choose not to exercise their rights, presumably believing they have little to gain by doing so. As Lindblom says: 'whatever the reasons, most people adopt a *rule* of performing an accepted task according to the task's specifications, and a *rule* of accepting the decisions of those to whom tasks have been assigned ... some of the rules they accept are those of obedience on specified matters to specified categories of persons, thus establishing the *authority* of those persons' (Lindblom, 116).

The elaborate division of responsibilities (divisions of labour, in the economists' jargon) serves two purposes in Lindblom's view: it raises the level of competence and, perhaps more important, limits the power and influence of any one policy-maker. Within the inner circle of that small fraction of the population directly involved, according to Lindblom, joint decisions are made: they are in-

structed not only by the general rules that hold for all participants, but by special rules holding for their particular roles; they use their authority over each other directly and indirectly; they persuade each other and reconsider their own policy positions. To facilitate joint decisions, the inner circle 'practise a variety of informal techniques for their mutual adjustment' (ibid., 117), as well as using formal organizations and procedures. Within this elaborate formal and informal system, those in the inner circle of policy-makers, and others wishing to influence them, use policy analysts as instruments in the battle to obtain the joint decisions they want. Policy analysis becomes a 'way of fighting over policy' rather than 'an alternative to the play of powers.' Says Lindblom, 'policy is analyzed not in an unrealistic attempt to reach conclusive determinations of correct policy, but simply to persuade. And it does not run afoul of disagreement on goals or values ... because it accepts as generally valid the values of the policy-maker to whom it is addressed' (ibid.).

From this point of view it follows that the leaders of interest groups, because they generally do not have any authority, must rely on their ability to persuade those in the inner circle by providing biased information. Because of the competition for office, they are forced to consider the tastes and preferences of the electorate, 'although parties try to attract votes by mere rhetoric and by irrational and nonrational appeals'; they also take policy positions 'that they believe, on investigation, to correspond to what the voter wants' (ibid., 118). The result is that party competition makes the elected members of the inner circle 'more responsive to the demands or preferences of relatively passive citizens than would be the case if citizens had to "signal" their wishes, with some positive action on their part' (ibid.).

In Lindblom's model, therefore, is a kind of pyramid, with the inner group of policy-makers at the top, interest-group leaders and political parties in the middle, and the citizens at the bottom. Between each level there is a two-way flow of information. The flow upward is designed to persuade those above to alter their positions on policy issues; the flow downward is designed to persuade those below to change their policy demands. The skilful leaders on the highest and secondary levels therefore have an opportunity to change policy by altering tastes and preferences or by changing perceptions of 'reality.'

Wildavsky

Aaron Wildavsky (1964) applies a Lindblom-type model of policy-making to the budgetary process in the United States. His conclusions about the role of PPB in general, and policy analysis in particular, are, as one might expect, quite negative. He points out forcefully the utopian nature of all normative theories of budgeting, including the pure theory of public expenditures:

> A theory that contains criteria for determining what ought to be in the budget is nothing less than a theory stating what the government ought to do ... A normative theory of budgeting would be a comprehensive and specific political theory ... Its accomplishment and acceptance would mean the end of conflict over the government's role in society ... The crucial aspect of budgeting is whose preferences are to prevail in disputes about which activities are to be carried on and to what degree, in the light of limited resources. The problem is not only how shall budgetary benefits be maximized? as if it made no difference who received them, but also who shall receive budgetary benefits and how much? (ibid., 128–9)

Wildavsky then states what has already been said earlier in this chapter, that assuming the existence of a welfare function 'in the absence of an ability to impose a set of preferred policies on others' is pointless because it amounts to assuming that agreement exists when it does not. Similarly, he argues that it is meaningless to assume that all citizens have the same tastes and preferences, for this would imply that all budgetary processes were, in effect, carried out by a single individual and that the problems of social conflict had disappeared.

In Wildavsky's opinion, and it is basically the same as Lindblom's, the budgetary process resolves conflicts '(under agreed upon rules) by translating different preferences through the political system into units called votes or into types of authority like a veto power. There need not be (and there is not) full agreement on goals ... Congressmen directly threaten, compromise, and trade favours in regard to policies in which values are implicitly weighted, and then agree to register the results according to the rules for tallying votes' (ibid., 130).

The budgetary decision-making process, in Wildavsky's view, proceeds, despite the inherent complexities involved in a perpetual 'war of all against all,' for three primary reasons: '[1] Only the small number of alternatives politically feasible at any one time are considered ... [2] These policies in a democracy typically differ only in small increments from previous policies on which there is a store of relevant information ... [3] Each participant may ordinarily assume that he need consider only his preferences and those of his powerful opponents since the American political system works to ensure that every significant interest has representation at some key point' (ibid.).

From such a position, it follows that PPB is bound to fail, because, at least in its more extreme forms, it would contravene each of these three principles. It also follows that if one wants to alter the outcome of the budgetary process (and why introduce PPB if the outcome is unchanged?) it is essential to change some fundamental aspects of the existing political system 'of which the budget is but an expression' (ibid., 131). Conversely, if one were to change the budgetary process so that it produced different outcomes, the political system would have been

fundamentally changed because some of the old winners would have lost and some of the old losers would have won. Whether such a change constituted an improvement would depend upon one's values. Were the old winners winning too much or the old losers losing too much? A change in the budgetary system that changes the outcome constitutes a change in the relative bargaining positions of the antagonists and predictably will be resisted by the old winners and advocated by the old losers.

The Lindblom-Wildavsky approach is inherently conservative. The decisions that emerge from a legitimate system are, by definition, legitimate. Both, however, acknowledge the possibility of improvement in the system. Lindblom, in looking at the policy-making process over-all, advocates what he calls 'reconstructive leadership,' with a leader who produces rolling compromises by gradually altering the preferences of individuals that constrain him.[7] Wildavsky says: 'My view is that the [present budgetary] process should be taken as far as it will go and then should be corrected for its worst deficiencies. Future proposals for reform should advocate a more thoroughgoing incremental approach rather than a more comprehensive one. There should be greater use of aids to calculation, rather than less. Agencies should not be told to give up advocacy but to make their best case more persuasive' (Wildavsky, 178-9). These directions of 'reform' are, it goes without saying, antithetical to PPB. Both Lindblom and Wildavsky are convinced that the specification of objectives is not possible, because ends and means are so closely intertwined, and not desirable, because it heightens overt conflict. Both are convinced that a synoptic view that considered simultaneously a large number of major policy changes is impractical because of the difficulties in predicting the consequences, given our lack of knowledge of consequences (uncertainty). Both emphasize that every political decision has a cost either in terms of precluding other decisions that are desired or by requiring other decisions that are not desired - the costs of negotiating an agreement among conflicting intervals. To force decisions through in the absence of a consensus or agreement where opponents are bought off could imperil the system. Both seek to minimize the conflict about values and rely upon the outcome of an advocacy process.

Let us now return to Charles Schultze, the PPB advocate, and briefly summarize his rebuttal. Schultze acknowledges that PPB, when effective, would alter the *political* process, or vice versa: 'Although PPB does not seek to replace the political decision-making process, it will - if successful - modify that process. And, equally, it must adapt itself to the essentially political nature of program deci-

7 By 'reconstructive leadership' Wildavsky means greater reliance on experience, simplification through line-by-line budgeting, satisficing, and incrementalism.

sion-making' (Schultze, 1968, 34). He also acknowledges that 'while incremental decisions make up by far the largest proportion of government decisions, ... they do not encompass the universe of decisions' (ibid., 77). When these non-incremental decisions are being reached, Schultze believes that PPB can play a useful role in widening the range of alternatives to be considered by focusing attention on the tradeoff between political salability and program effectiveness. He does *not* advocate that analysts ignore politics, and indeed points out that the final decision is likely to be the second, third, or even fourth alternative from the analysts' point of view. But he insists that someone should put the effectiveness side of the question.

In theory, at least, PPB implies 'zero base reviews' on a regular (annual?) basis of all programs. A zero base review is nothing more than a review starting from the assumption that a program does not exist, or at least could be dropped or extensively modified. It is, in other words, the antithesis of incrementalism, which starts from the assumption that virtually everything that exists will remain and only small (usually positive) changes are worth considering. It is Schultze's opinion that it is unworkable to carry out a zero base review of every program every year. He admits that as director of the budget he asked for too many special reviews, given the resources available to carry them out or interpret the results. He is now a strong believer in selectivity – following the incremental approach most of the time for most of the programs but examining a few existing programs in depth each year. 'Incremental budgeting alone – especially when confined to a single budget year rather than a multiyear plan – tends to deny the President, his immediate staff, and his cabinet officers the opportunity to review a significant range of alternatives. It confirms the inertia of existing program arrangements and budgetary allocations and strengthens the power of subordinate bureaus and offices' (ibid., 81).

Schultze has some interesting things to say about the strategy to be followed in selecting programs for intensive review. But this need not detain us. What is important, from our perspective, is his awareness that PPB becomes part of the advocacy process, not a substitute for it. 'Systematic analysis complements the advocacy process by articulating the links between general values on the one hand and specific program characteristics on the other. It is in tension with political dialogue because it emphasizes resource efficiency and stresses economic opportunity costs, while political dialogue has its own set of efficiency criteria and emphasizes political opportunity costs' (ibid., 92). And further on he states: 'Decision-making is done by advocacy and bargaining. PPB introduces the 'efficiency partisan' into the debate' (ibid., 95).

All of this raises the question, of course, about the power base from which policy analysts are admitted to and participate in the decision-making process.

Why should anyone in the system listen to them? What motivates the analysts to do battle? Although Schultze says little about it, he conveys the impression that each agency will have a PPB unit within it responsible directly to the agency head. The latter will use the unit to gain power at the expense of the operating units in his own agency. The PPB units in agencies will themselves gain power because they will have the support of the Bureau of the Budget. That is to say, the Bureau will squeeze agencies that do not provide adequate analyses, and this will entail that agency heads will have to take PPB analysts seriously. It should be noted, however, that the power position of PPB analysts under this scheme is largely dependent on the power of agency heads and the Bureau of the Budget. If an agency head cannot, in the event, deny finances and real resources to his operating units when they refuse to co-operate in carrying out analyses, or when the results are negative, the PPB unit in the agency will have a weak voice at the bargaining table. Similarly, if the Bureau of the Budget has little impact on the allocation of resources among agencies, even when the analytic results (or lack of them) would strongly suggest some changes, the PPB unit will have no credibility with agency heads.

Schultze has two interesting chapters that consider the vitally important questions of designing into programs the appropriate incentives: rewards and penalties. He does not, however, discuss the incentives under which the practitioners of PPB act. The policy analyst seems to be an individual who is either motivated to fight the good fight because of his own personal standards or because his job requires him to play the role. Nothing is said about the self-interest of the analyst.

SUMMARY OF FINDINGS AND IMPLICATIONS

What clearly emerges from this admittedly sketchy review of the literature is that there is no received conceptual framework within which to analyse and assess alternative expenditure budgetary processes. What also clearly emerges is that the development of a greater understanding of this process is an essential step in the development of a predictive theory of government expenditures. This is not to say that the intellectual cupboard is bare. A great deal has been thought and written that is germane to our subject. Even welfare economics and the pure theory of public expenditures, although normatively oriented, serve to clarify concepts and clear away the underbrush. But having said this, it remains true that the task of integration of what already exists remains to be done, although Breton has certainly gone some distance in that direction. Let us recapitulate what we have discovered in order better to see what is missing.

None of the so-called grand theories have anything to say about the decision-making process, although several of them imply that there are psychological or institutional factors at work that strongly affect the outcome.

The theory of market failure seeks to develop a framework within which economists could derive policy evaluations that would be accepted by those who accept the 'one or more individuals better off and none worse off' criterion of Pareto optimality. Based on this criterion it is possible to derive an elegant rationale for government intervention to offset or compensate for externalities, both positive and negative. But of greater relevance for our purpose is the insight that transaction costs probably play a crucial role in the determination of the institutional structure, which in turn affects all private and public decisions. When economists assume a world of perfect, costless information, and hence no uncertainty, they are assuming away a large part of the problem.

The pure theory of public goods is an elaboration of the theory of market failure. Much of the work in this field is devoted to deriving the consequences that follow logically from the specification of a social welfare function that provides a standard against which to assess all conceivable states of society. By assuming the existence of such functions, economists have been able to isolate economics from politics. This division of labour has undoubtedly led to more theoretical depth and elegance for economics, but there have been substantial costs. If the concept of the social welfare function were an ingenious simplification of reality that made it possible to derive testable predictions there would be no quarrel with its lack of realism. Unfortunately such is not the case. Conceivably a small group of like-minded individuals could define some crude kind of social welfare function, although it is difficult to imagine how this could be done given the intrinsic difficulties of spelling out *all* objectives (and thus constraints). When tastes and preferences differ, as they always do, the task would be that much more difficult because strategic behaviour would come into play. What would motivate the members of the group to agree to resolve all of their differences simultaneously at a particular point in time?

The collective decision-making theorists emphasize the importance of decision-making rules rather than the individual decisions made within those rules. They also emphasize that the rules are what they are because individuals follow their self-interest. These are most important insights, about which more will be said later. This work has, however, several limitations:

- Buchanan and Tullock in particular, but the same is also true of Downs, Olson, and Niskanen to some extent, are preoccupied with the development of normative theories. They seek to define the conditions under which the decision-making rules of organizations would be optimal. One might have wished that they had placed greater emphasis on the positive (predictive) side of the question.
- There is, at any point in time, a hierarchy of decision rules. At the top of the pyramid is the set of rules known as the constitution. Under this set, and derived from it, is another extremely large set of rules known as laws. Under this set, and

derived from it, is another set of almost infinite size consisting of regulations, and so on. Some are formal, others are not, although often equally binding; some are consistent, though others are not, and there are rules for dealing with inconsistencies when they arise. Although they disclaim it, Buchanan and Tullock write as though a large group of individuals in a state of nature were deciding on optimal sets of each kind of rule simultaneously. In fact, of course, the only relevant issue at any point in time is changing a few rules within an existing structure.

- Breton's approach involves changing one of the variables at a time (including a particular decision rule) and working out the consequences - a new equilibrium. This is clearly superior to the Buchanan and Tullock assumption that everything is up for grabs at every point in time. But it does not take into account systematically the never-ending series of compromises that characterize much of political decision-making.
- There is a difficult conceptual problem in relating the utility functions of the individual politicians (and bureaucrats) to the utility functions of individual voters. One 'solution' is to assume that all members of the governing party have identical preferences. Another is to assume that they negotiate to produce a common utility function. Still another is to ignore political parties altogether and to assume that individuals (voters) essentially negotiate with one another. None of these approaches is altogether persuasive. The first two, at least, are tantamount to the introduction of a social welfare function through the back door, with all that that involves. The latter is equivalent to assuming that politicians and bureaucrats are passive intermediaries.
- There is little if any explanation why some individuals become politicians, some bureaucrats, others interest-group leaders. Nor is there much room left for the influence of different personalities in the same role.
- Some of the authors (Breton in particular) emphasize the strategems that the governing party uses to gain manœuvring room. But there is no explanation of how this freedom is used when it is acquired.
- The theory of voluntary organizations seems to be well developed and poses few problems.
- The theory of bureaucracies is much less convincing. There is really no explanation of their bargaining power relative to the governing party. They are simply assumed to possess it. Yet this bargaining power plays a crucial role in several of the theories advanced. The discussion of the uses of monopoly power by bureaus, and of their lack of incentive to reduce costs, is more persuasive.
- Breton has argued that it is useful to look upon the decision-making process in terms of the demand for and supply of public policies. One cannot keep wondering if this ingenious simplification does not hide the fact that it is the *effects*

of policies – changes in personal satisfaction through government actions – that are demanded and supplied. Different policies have widely different effects – policies are not a homogeneous good.

– He has also argued that some may look upon a particular policy as a means while others consider it an end in itself, with the result that disputes arise about its efficiency. But surely all policies are means: controversy arises largely because there are different evaluations of the multiplicity of effects.

– Some important rules that shield politicians from other preferences have not been taken into account, such as the determination of electoral boundaries, campaign financing, and the laws of secrecy.

– That individuals may engage in political action when they feel coerced (the value they assign to what they get from government falls short of the tax costs they are compelled to pay for it) seems reasonable. But surely whether political action is actually engaged in depends upon the expected return on the investment of time and effort. Furthermore, when the rate of return on political action looks attractive, will not individuals who do not feel coerced seek to improve their position, even if this means coercing others?

– Breton has developed a useful inventory of the techniques that a governing party has at its disposal to reduce (or increase!) coercion.

– The econometric analysis of the changes in government expenditures has not yet succeeded in explaining 'shift points.' Yet it is these shift points that must be explained in order to explain the dramatic changes in the size and composition of government expenditures in the longer run.

Program planning and budgeting has much in common with the theories of market failure and public goods. Here too, the advocates assume away much of the problem. The information assumed to exist does not exist, and much of it cannot be obtained, even in principle. Furthermore, politicians and bureaucrats are treated as all-knowing altruists, who have no personal ambitions that are inconsistent with the public interest, somehow defined. No recognition is given to the rules that allocate power and responsibilities. The process takes place in an organizational vacuum.

The pragmatic incrementalists are realists. They accurately *describe* the decision-making system as it is in the United States, as even the PPB advocates acknowledge. Their limitation is that they cannot explain how the system became as it is, nor can they adequately account for why it changes.

It would be wishful thinking of the highest order to suggest that all of these limitations – both gaps and inconsistencies – could be easily corrected in *any* single work, much less in this brief study. However, perhaps a modest beginning can be made at an integration of some of the insights previously described. Selecting a particular issue – the budgetary process – may provide a needed focus.

It has long been the author's view that the economists' assumption that individuals make decisions in order to maximize their self-interest, as they perceive it, is extremely useful. This review of some of the literature concerned with collective decision has reinforced that opinion. However, many non-economists seem to find the concept either empty or repulsive; some economists, on the other hand, seem to interpret individuals' self-interest too narrowly. The next chapter seeks to provide an exposition of the concept that will help to resolve some of these difficulties. The concept of self-interest developed there is the foundation upon which the theory sketched in chapter 3 rests.

2
The meaning of self-interest

There seems little doubt, based on the review of the literature contained in the previous chapter, that the group of authors who have adopted the self-interest postulate have come closer to the development of a meaningful theory of the expenditure budgetary process than any of the others. The grand theories are too grand; they seek to explain everything and hence explain nothing. The theories of market failure and the pure theory of public expenditure provide an elegant rationale for a group of decisions that are not really in dispute except with respect to the magnitudes involved - about which the theories are largely silent. The program planning and budgeting analysts seek to make normative statements that are unlikely to be convincing except to those who are already convinced. Pragmatic incrementalism is more a description of reality than an explanation of it.

The assumption that individuals seek their own interests is one of the fundamental pillars of the discipline of western economics. As suggested above, the basic assumption is often found to be offensive to non-economists because it strikes them as crass, materialistic, and lacking in an awareness of the finer virtues. Economists, to be sure, have invited this criticism, at least in part, by constantly talking about money or the things that money can buy. This is understandable because the measuring rod of money is, in a peculiar sense, concrete. By ignoring transactions where barter rather than market prices prevail, economists have been able to make great theoretical strides relative to the other social sciences in terms of elegance and, to some extent, predictive power. The problem is that some of the fundamental insights of economics (in particular the maximization of self-interest and the notion of opportunity cost) have seldom been applied to non-market problems where they might well be helpful. Stripped to the essentials, economics is a theory of decision-making, not a theory of money.

There are, obviously, an infinite number of non-market decisions made every day. Some of these decisions are at least as important as market decisions: indeed, many of them dominate market decisions. It is our view that economics has something useful to say about these non-market decisions.

It is assumed (although one is sometimes tempted to deny it) that politicians, bureaucrats, special-interest group leaders, and journalists – the principal participants in the budgetary process – are human. They follow their self-interest neither more nor less than the average voter. What differentiates them from the average voter is not their selfishness but rather the particular incentives and disincentives that apply within the unique games within which each group operates. Another factor may be the selection procedures, which exclude from each of these occupations not only those who do not have the requisite inherited or acquired talents (e.g. a comparative advantage in discharging the functions of the occupation) but also those who are unlikely to be willing to abide by the formal and informal rules that constitute its incentive system.

Politicians, bureaucrats, interest-group leaders, and journalists behave differently from one another, and from the average voter, in part because they have different talents; but as rational, self-interest seekers they respond to the special incentive systems prevailing in their several environments.

BASIC PROPOSITIONS

Definitions are, of course, inherently arbitrary. They can be judged good or bad only in terms of their degree of usefulness in dealing with a particular problem. The definitions given below are only put forth on the basis that they seem to capture most of the interests of individuals that are relevant to the issues at hand.

The first and most fundamental proposition is that *all* individuals seek to maximize their utility (satisfaction). This does not mean that they spend most of their time calculating minute personal advantages. Only when the expected gains are believed likely to exceed the expected costs of obtaining them do rational individuals acquire information, negotiate terms, and try to enforce their rights. Nor does it mean that individuals necessarily seek to maximize their money incomes. There are, as explained below, other sources of utility that may accord a higher return on the investments involved.

The second proposition is that, at any point in time, the utility (satisfaction) of the individual is determined by four factors: the current and expected future flows of utility to be derived from the consumption of tangible services (including the services provided by goods);[1] the current and expected future flows of

1 Tangible services comprise: 'own' services, including leisure; the services of others, including public services; the services of goods and facilities, including public facilities.

utility to be derived from psychic income;[2] the current and expected future flows of utility that the individual must forgo (disutility) in order to obtain the first two; the timing of all of these flows.

By casting all three flows in present-value terms, and subtracting the last item from the sum of the first two, we obtain the desired concept: the utility of the individual as he or she perceives it at that point in time. This concept, for want of a better name, is termed 'subjective net worth.'

The sources of the individual's flow of utility are, of course, his or her assets, The individual's obligations to provide flows of utility to others (or the sources of such flows) are his or her liabilities.

DEFINITION OF SUBJECTIVE NET WORTH

Let us now try to define, albeit in an arbitrary manner, somewhat more precisely what we mean by the terms assets and obligations (liabilities), which determine the subjective net worth of the individual.

Assets are, in essence, property rights. Usually they exist because other individuals accept an obligation (liability) to provide, or are forced by the state to provide, a flow of utility (directly or indirectly) to the person or persons who holds them.[3] It seems useful for the present purpose to differentiate six classes of assets. In principle, every source of utility to an individual falls into one of these categories.

1 Residence in a particular municipal, provincial, and national jurisdiction that is perceived to possess, to a relative degree dependent upon the knowledge, tastes, and preferences of the individual, bundles of characteristics that are sources of utility to those who live there. Some of the more obvious bundles of

2 Psychic income comprises, among other things: personal pride (self-esteem), which is determined by the individual's perception of the extent to which his own characteristics conform to his own standards; personal prestige (status), which is determined by the individual's perception of the perceptions of others about the extent to which his characteristics conform to their standards. (Prestige is a question of rank – a zero sum game in which the winners displace the losers.) For a discussion of characteristics in demand theory see Lancaster (1966).

3 Public goods are the exception to the rule that one man's asset is another man's liability. A favourable climate gives those who live under it a flow of utility (or to put the matter the other way, they avoid the disutility of living in a harsh climate). A favourable climate is clearly an asset that does not generate a corresponding liability (except for God!). Other public goods, such as defence services, provide a flow of utilities and are hence an asset to the individual. But the same asset enters into the subjective net worth of many individuals. Here, one man's asset is also another man's asset. There is, in the case of defence, a single liability that is allocated among the taxpayers.

characteristics are physical (weather), demographic (population density), socio-cultural (language), politico-legal-economic (freedom of speech), and public goods and services (security of persons and property). These characteristics are the 'pure public goods' of public finance theory.

2 Memberships in informal groups or formal associations that afford one or all of the following: pride of membership, prestige of the member in the eyes of other members, prestige of the member in the eyes of non-members, income in kind including the ability of the group or association to influence government decisions, the services of physical facilities (e.g. a club house), and money income (e.g. strike pay).

The following kinds of groups or associations are involved: parental families that bestow membership in informal racial, ethnic, linguistic and religious groups; marital families; recreational and social clubs; trade unions; trade associations; occupational groups; and political parties.

3 Tenure of offices or employments that afford the current incumbent, or those who were incumbents, one or more of the following: pride in the possession of relative power or influence; prestige within the organization based on the perceived relative power and/or influence of the individual over his subordinates or over the collective decisions of the organization; prestige outside the organization based on both the perceived relative power or influence of the individual within the organization or the perceived power or influence of the organization itself; money income; income in kind (the prerequisites of the office or employment).

4 Marketable assets that afford the owner pride both in the possession of the power to gratify his own wants or the wants of others, prestige from those who are impressed with this, money income, or income in kind that saves the pocket (e.g. home ownership).

5 Entitlements to benefits under government programs for which the individual qualifies by virtue of his specific characteristics over and above residence per se. These entitlements usually generate money income (e.g. family allowance payments) or income in kind (e.g. medical services).

6 Human capital: the strength, skills, and knowledge that can be consumed as leisure or used to meet the requirements of memberships or tenures or invested in requiring or trading assets or liabilities.

Liabilities include financial obligations (e.g. direct taxes) and obligations to provide flows of 'own' services or income in kind or the use of a facility as a condition of a membership or tenure. Perhaps the most obvious example is the husband and father who is obligated, in part by law and in part by custom, to provide his wife and children with money, time, effort, accommodation, and so on. The employee has an obligation to provide services as a condition of the tenure of his job. The costs of maintaining one's own human capital, such as the cost of

TABLE 1
Individual wealth: a comprehensive formulation

Assets and claims [present value (PV) of expected lifetime benefits]	Liabilities and obligations [present value (PV) of expected lifetime costs]
Marketable assets	*Financial liabilities, not elsewhere stated*
Dollar value of current holdings	
PV of expected imputed income in kind	*Other obligations*
PV of expected imputed psychic benefits	To relatives and other individuals
derived from perceived prestige based on	PV of expected dollar outlays
conspicuous wealth or market power[1]	PV of expected imputed outlays in kind
	PV of expected imputed earnings or leisure
Human capital	forgone
Gross return	PV of expected imputed psychic costs in
PV of expected earnings	conforming to behavioural standards of
Dollar amounts	others, less psychic benefits (pride) in
Imputed income in kind	conforming to own behavioural standards
Imputed psychic benefits derived from	To governments (local, provincial, and federal)
prestige, esteem, and pride associated	PV of expected dollar amounts of taxes and
with the individual's occupation[2]	losses resulting from expropriations
PV of expected 'leisure'	PV of expected imputed earnings or leisure
Imputed earnings forgone	forgone under conscription
Imputed psychic benefits derived from	PV of expected imputed psychic costs in
prestige associated with conspicuous	conforming to law, less psychic benefits
indolence	(pride) in conforming to own behavioural
Deduct	standards
PV of expected 'subsistence'	To voluntary associations
Dollar costs	PV of expected dollar outlays
Imputed outlays in kind	PV of expected imputed outlays in kind
Imputed earnings or leisure forgone	PV of expected imputed earnings or leisure
PV of expected education costs	forgone
Dollar costs	PV of expected imputed psychic costs in con-
Imputed outlays in kind	forming to behavioural standards of the asso-
Imputed earnings or leisure forgone	ciations, less psychic benefits (pride) in con-
Imputed psychic costs in conforming to	forming to own behavioural standards
educational standards	
PV of expected health costs	*Net worth*
Dollar costs	
Imputed outlays in kind	
Imputed earnings or leisure forgone	
Imputed psychic costs of pain and suffering	
Claims to transferred benefits specific to the individual	
From relatives and other individuals	
PV of expected dollar receipts	
PV of expected imputed receipts in kind	
PV of expected imputed psychic benefits derived from prestige, esteem, or affection accorded the individual by relatives or other individuals	
From governments (local, provincial, and federal)	
PV of expected dollar receipts	
PV of expected imputed receipts in kind	
PV of expected imputed psychic benefits derived from prestige or esteem accorded the individual by governments	

TABLE 1
(concluded)

Assets and claims [present value (PV) of expected lifetime benefits]	Liabilities and obligations [present value (PV) of expected lifetime costs]
From voluntary associations	
PV of expected dollar receipts	
PV of expected imputed value of receipts in kind	
PV of expected imputed value of psychic benefits derived from the prestige or esteem accorded the individual by the other members of each group of which he is a member	
Claims to share in collective benefits	
PV of expected imputed benefits derived from the common property of each of the groups of which the individual is a member: family, neighbourhood, community, region, nation, world, voluntary associations, racial-ethnic-linguistic	
Common property includes:	
Quantity and quality of unappropriated natural resources including air, water	
Access to stock of knowledge and the quantity and quality of that stock	
Access to social, cultural, and recreational activities and the quantity and quality of such activities	
Availability of privacy	
Prestige of the group in the eyes of non-members, based on the power of the group to influence the decisions of other groups	
Esteem of the group in the eyes of non-members, based on conformity of its behaviour to their standards	
Pride of the members of the group in the group, based on conformity of its behaviour to the standards of the group	

NOTE: In principle, all dollar values are deflated by the expected prices of the basket of goods and services the individual would purchase. Wealth is expressed, therefore, in terms of real purchasing power.

1 Psychic benefits and costs are subjective and not capable of objective evaluation. Psychic benefits from prestige or esteem depend upon the perceptions of the individual about the perceptions of others and are doubly subjective.

2 Prestige is defined as the perceived favourable attitude of others arising from the perceived influence of the individual in allocating rewards and punishments to others. Esteem is defined as the perceived favourable attitude of others derived from the perceived conformity of the behaviour of the individual to their standards. Pride is defined as the sense of satisfaction enjoyed by the individual, achieved through conforming to his own behavioural standards.

food, clothing, and shelter, can also be looked upon as a liability, or alternatively one can treat the asset of human capital on a net basis – after deducting maintenance costs.

This completes the definition of subjective net worth. It is recapitulated in Table 1, which sets forth the basic elements in traditional form.

While it should be obvious, this formulation of subjective net worth does not purport to be operational. It would be pointless for one individual to seek to make a quantitative estimate of the subjective net worth of another individual, because many of the components do not have market prices. To assign a dollar value to some of the assets and liabilities in another individual's portfolio (the value of the degree of security of persons and property, for example) would be to assert a knowledge of what cannot be known except to the individual. At best such imputations would be unconvincing. At worst they would be looked upon as plain silly. Subjective net worth is a conceptual framework, not a form with blanks to be filled!

DETERMINANTS OF CHANGES IN SUBJECTIVE NET WORTH

How are assets and liabilities acquired or disposed of? There seem to be two basic methods: by investing in the acquisition of assets (or the reduction of liabilities) current flows of money, income in kind, or 'own' services; and by windfall gains and losses, including gifts and inheritance, changes in relative prices because of market forces, changes in government policies over which the individual has no influence, and all other exogenous changes.

The total utility of the individual is maximized at a point in time when, *having taken transactions costs into account*, he cannot gain additional utility by changing the composition of his current consumption, the level of his current consumption relative to his investment in additional assets, or the composition of his portfolio of assets and liabilities. Having achieved such an optimum, windfall gains are the only source of an increase in the individual's subjective net worth.[4] Subjective net worth can, however, be reduced in two ways: by windfall losses and by depletion. Depletion necessarily occurs with 'the business of living' – death approaches.

4 This leaves aside the increases that might arise when the expected flows of utility and disutility are cyclical and not in phase. The passage of time, under these circumstances, could mean that subjective net worth has a cyclical pattern, presumably around a dictating trend, over a lifetime.

IMPLICATIONS

Several implications of this formulation of the interest of individuals that are particularly relevant for the present purpose should be noted. The assets identified are not independent. That is to say, an individual cannot choose simultaneously to reside in the south of France, be the mayor of a Canadian city, and be entitled to the benefits of an American citizen. The value of assets is dependent upon perceptions, upon *expected* flows of utility. Changing perceptions through the provision or withholding of information can generate windfall gains and losses. The value of assets and liabilities to the individual is dependent upon personal discount rates (the individual's time horizon) and upon the timing of flows of costs and benefits. Benevolence is *not* inconsistent with the pursuit of self-interest, because utility is derived from personal pride (behaviour consistent with own standards) and prestige (behaviour consistent with the standards of others).

It is apparent that government decisions can affect the utility of the individual both positively and negatively in a host of ways. Among the more intangible, more indirect, or more collective effects are changes in the quantity and quality of the public goods available in the area where the individual resides (the security of persons and property), changes in the terms of tenure of an office or employment, and changes in the relative prices of goods, services, and marketable assets.

If, as we assume, individuals act so as to maximize their utility, and if governments can affect their utility in such diverse ways, how would we expect them to behave toward governments? There are many alternatives. They can 1/ do nothing; 2/ vote for that party most likely to implement the bundle of policies that they perceive will increase their subjective net worth the most or reduce it the least; 3/ in addition seek actively to change government policies through the application, directly or indirectly, of threats or bribery or persuasion either as an individual or as a member of an association; 4/ move from one jurisdiction to another; or 5/ adopt some combination of the last three steps.

Associated with each alternative course of action is a whole range of possible scenarios. And associated with each possible scenario is a whole range of subjective net worth estimates for the individual. What each voter requires, in principle, is an infinite number of benefit/cost analyses, each taking into account a multiplicity of contingencies because strategic behaviour by all parties is not only possible but probable. Yet consider the kinds of information the typical voter has at hand. He has certain perceptions of the way in which his subjective net worth has changed in the past. Asset A increased slightly in value; asset B decreased substantially; liability C increased dramatically; and so on. But to what extent

were the improvements attributable to the policies of the government in office? To what extent could the deteriorations have been prevented by the government in office? What would the changes likely have been had the other party been in power? Except when considering changes in direct taxes or transfer payments (even here, shifting confuses the issue) or tangible services provided to specific individuals, it is extraordinarily difficult to determine, even retrospectively, the 'real' impact of government policies. Despite this basic ignorance, the voter is required somehow or other to appraise the prospective performance of competing political parties. Small wonder that they take short-cuts: vote ideologically (labels), or for 'a personality,' or for a 'native son,' or not at all!

In deciding how to vote (including abstention) or whether to incur the costs of supporting or organizing pressure groups or the heavy costs of moving to another jurisdiction, the individual has precious little hard information available. Obtaining additional hard information is costly. Therefore, unless potential changes in government policies are perceived by the individual to be likely to have a large and direct impact on his utility and to be subject to change at a cost that is less than the prospective benefit, it is rational for him to follow some rule of thumb in voting, pay little attention to pressure-group activities, and ignore the possibility of moving to another jurisdiction.

What is an individual's optimal investment in additional information, given that it is only on the basis of the information itself that he can determine the potential additional benefits to be obtained from it? This is an unanswerable question. But it is likely that those who are well educated and in touch with people 'in the know' are much better able to take an informed gamble.

While there is, as we have said, little hard information available on which to base political decisions, there is a surfeit of soft and biased information. Acquiring, sorting, and storing this information is costly. In self-defence, individuals probably develop a relatively high perceptual threshhold. They simply ignore much of the soft information available unless it involves dramatic changes. After a short time, they discard much of the stored information if it has not been used to their advantage. They have, in other words, short memories.

Most individuals also seem to have relatively short-term horizons. This, no doubt, is in part because of uncertainty. While their personal discount rate for a benefit that is certain may be, say, 10 per cent in real terms, they may well attach a risk premium that doubles or triples this rate to a promised benefit from a government.

Individuals seem to adjust their expectations relatively quickly. Actual changes in government benefits apparently are soon capitalized and become 'rights' to utility. The converse apparently holds for government costs; they become, in a relatively short time, accepted obligations.

What does this imply for the behaviour of governments? Manipulating public expectations is extraordinarily important. This can be done by supplying hard or soft (biased) information or by withholding hard information. And the shorter the memories of individuals the less important are broken past promises, and the lower the rate at which they will discount current or prospective promises. The present value of an expected future benefit promised by a credible government will be much higher than that of one promised by a government that cannot be trusted to honour its pledges. To a considerable degree, credibility is a matter of memory!

Timing is of the essence: the magic of compounding means that by promising immediate benefits and postponing costs, a prospective program can be made more attractive to the voter. No doubt this is the reason ministries, once elected, try to get the unpleasant decisions made as quickly as possible and leave the pleasant ones until just before the next election.

Although casting a vote is seldom costly to the individual (a little time and discomfort perhaps) thinking through whether or not to vote, and if so for whom, can be extremely costly in terms of time and mental energy. The result is that many individuals appear to adopt rules of thumb. The first rule is that they will always vote so that they do not have to think about the likely impact of one more vote for a particular candidate. Secondly, they decide they will vote for a particular party (or leader) at least until something sufficiently dramatic happens, or is expected to happen, that will lead them to reconsider this rule. The wider this 'band of indifference,' or better, 'insensitivity,' the more cavalier the government of the day can be with its committed supporters, and the more difficult it is for opposition parties to entice them away. This suggests that the optimal strategy for a ministry seeking re-election will often be to spread the costs widely so as to take a little from the committed supporter and to concentrate the benefits on the others, particularly those who are either uncommitted or at the margin of their band of indifference in their attachment to another party.

Pressure group activities can be looked upon as a kind of investment by the individual designed to obtain favourable government decisions that mean either increased assets or reduced liabilities. This suggests that governments can discourage these kinds of investments by raising the costs (e.g. requiring elaborate briefs) or by reducing the perceived likelihood of success.

Credibility is a double-edged sword. The more credible a ministry, the less it has to promise in the way of increased benefits or reduced costs in order to obtain a given effect on the subjective net worth of the voter. It also means, however, that current programs are capitalized at a relatively low rate of interest (risk of change is small) unless they were adopted by another party while in office or were attacked by the party currently in power before the preceding

election. This makes it extremely difficult to remove existing benefits because they are extremely valuable to those receiving them. The same is true of the imposition of unexpected costs by a credible government.

In conclusion, a few similarities and differences between the formulation in this chapter and the views of other writers should be drawn to the reader's attention. The concept of subjective net worth developed here is very similar to, if not identical with, Anthony Downs's concept of the voters' 'utility income from government activity' (Downs, 1957, 38) put into present-value terms. Capitalizing the expected flows highlights the importance of timing without losing the important insight that uncertainty (information) is of crucial importance. The implications are therefore not inconsistent, although some not mentioned by Downs are derived in a non-rigorous manner. The subjective net worth concept does not seem to have any parallel in Breton's theory. Rather, it will be recalled, he uses the concept of 'coercion' to explain the political behaviour of the voter (or its absence). When not coerced, the voter will support the governing party in Breton's view. As argued above, this is roughly equivalent to the assertion that voters are satisfied when the bundle of government policies, including taxation, leaves them as well off as they would have been in their absence. The formulation in this chapter emphasizes rather that individuals will act to maximize their utility through political activity, a quite different notion.

3

A new perspective on the expenditure budgetary process

This chapter attempts to set forth some parts of a crude model of the expenditure budgetary process, drawing upon the concepts previously introduced of self-interest, transactions costs, and decision rules. Perhaps the fundamental idea can best be explained by way of an analogy. Each individual seeks his or her self-interest, broadly defined. Individuals have to compete for membership on a team and with the members of that team for advancement within it. The teams playing the same game also compete with one another.

Four distinct games can be differentiated: the political game, the bureaucratic game, the special interest group game, and the media game. Each game has its own set of rules. These sets of rules constitute the incentive systems under which the individuals and teams operate. They determine the basis on which players are selected and on which teams are admitted to the particular game. The rules also specify actions that score points and those subject to penalties.

Complex exchange relationships exist among players of the same teams, among teams in the same game, and among the several games. These exchange relationships can be positive (bribery) or negative (blackmail). The former involves the voluntary exchange of one advantage for another; the latter involves obtaining an advantage in exchange for *not* imposing a disadvantage. Blackmail is voluntary only in the sense that the 'victim' would rather surrender the advantage than bear the disadvantage but would, of course, prefer neither.

A coalition (alliance), which can be a formal agreement or simply an unspoken understanding, is a particular kind of exchange relationship in which the parties (individuals or teams) agree to act in concert for their mutual advantage (or to reduce their disadvantages). It is usually understood, though often not explicitly stated, that when the sharing of the gains (or reduced costs) flowing from a coali-

stated, that when the sharing of the gains (or reduced costs) flowing from a coalition is too one-sided, the coalition agreement will be terminated unilaterally by the party that perceives itself to be the loser in the exchange – bearing in mind possible retaliation.

The expenditure budget can be looked upon as a temporary resolution of the competition within and between all teams and all games. It reflects such things as the quality of the players selected by each team, the prevailing rules, and the relative abilities of the participants to drive hard bargains in the multitude of exchanges that take place.[1]

The rules are important for three reasons. First, they constitute a part of the incentive system and hence influence individual and collective actions. Second, they confine the conflict between competing individuals and teams and hence maintain the stability of the system. Third, they legitimize decisions that are inherently arbitrary.

Because information is costly (indeed, some of it is not obtainable at any price), because many of the interests of individuals are in conflict, and because a universally accepted standard by which to resolve these conflicts is not possible, budgetary decisions are necessarily founded on partial ignorance and will, implicitly if not explicitly, coerce some of the electorate. There are always losers, at least in the sense that the expectations of some individuals are disappointed. The existence of generally accepted rules governing the process legitimize the decisions that emerge from it. These rules ensure that most of those whose interests are affected have their day in court and an opportunity to exercise their bargaining power in a legitimate manner. Another and more important result is that the losers under particular budgetary decisions acquiesce in their losses unless they perceive that they are likely to be perpetual losers and can only gain through revolutionary change, that is, through behaviour that is not acceptable under the prevailing rules.

The next three sections set forth the rules and conditions under which each of the particular games are played. Further sections try to specify these rules and conditions as they apply to the budgetary process itself. The final chapter sets forth a few propositions that might be tested in a non-rigorous manner by case studies, the detailed examination of particular expenditure decisions.

It cannot be emphasized too strongly that the purpose is to present a way of looking at the process rather than a rigorous model that can be used to derive quantitative predictions of the outcome of changes in that process. It is doubtful that such a model can ever be developed, for it would mean, to all intents and

1 It should be pointed out that the bargains are tough in the sense that poker is tough. Bluffing is an accepted strategy, as is taking advantage of your opponents' emotional and intellectual weaknesses.

purposes, that the analyst could anticipate many of the events of which history is made: electoral outcomes, the influence of leadership and hence personalities, changes in public perceptions and attitudes, interest-group tactics, and so on. Were the analyst to acquire this much knowledge and understanding, life would hardly be worth living, for it would imply that everyone was programmed to the point where personal choice was meaningless.

THE RULES AND CONDITIONS OF THE POLITICAL GAME

Elected offices seem to provide five basic kinds of benefits to those who hold them (not necessarily listed in the order of their importance): income in kind (perquisites of office); increased personal pride derived in part from the attainment of the office as such and in part from perceived achievements while an incumbent of the office; personal prestige derived from the possession and effective use of power and influence, as perceived by others; acquisition of a knowledge of 'the system' and of the skills needed to deal with it (e.g. negotiating skills); and acquisition of the right to favours from participants in the system in exchange for favours previously delivered to them.

Obtaining elected office usually involves some onerous costs. These include the investment of own time, effort and money in acquiring prestige (sometimes called 'creating an image' or, in an earlier era, 'building a reputation') and negotiating the terms of support; putting at risk a currently held office or employment; putting at risk a reputation derived from having successfully filled prestigious offices or employments in the past; and accepting obligations to provide favours to others at a later date, if and when office is achieved, in exchange for immediate support. Casual observation suggests that elected office, once obtained, usually imposes additional costs: there is a sacrifice of money income, leisure, and privacy.

Under our formulation these investment and operating costs are only incurred because there is perceived to be a reasonable probability that they will be more than offset by the subsequent flow of increased benefits. Most politicians presumably do not enter the game as a means of acquiring something to sell in what might loosely be called the private sector game. Nevertheless, the fact that intangible assets can be accumulated while playing the political game probably explains the willingness of some individuals in some occupations to run the risk of seeking public office.[2] One thing seems reasonably certain: because there are these indirect benefits, it is not necessary to assume that it is only because of the likelihood of gaining the perquisites and the psychic income of elected office that individuals decide to become politicians.

2 Notably lawyers, journalists and consultants.

It is a rare occasion indeed when it is in the interest of the individual politician to be personally defeated rather than elected, or to be an elected member of the minority rather than the majority party, or to be a backbencher rather than a minister, or to be a minister with a trivial rather than an important portfolio, or, finally, to be a minister with an important portfolio rather than the prime minister or premier. It is therefore assumed that those who chose to become politicians have the following objectives in approximately the order given: to get nominated as the candidate of the majority party; to get elected; to be appointed a minister; to acquire the most prestigious portfolio; and to be appointed the leader of the party (and therefore become prime minister or premier).[3]

For reasons that are not entirely clear, explicit statements of these objectives are abhorrent to some. Few are alienated when a businessman states that he wants to maximize his profit. While hard to document, a politician who admits to wanting to be elected, stay in office, and rise to the highest of offices seems to be thought to be unprincipled and opportunistic by the electorate. Two reasons can be offered for this apparent inconsistency. Politicians operate within their own set of rules, which in effect, legitimizes certain kinds of behaviour within the political system that are considered illegitimate outside of that system. For example, vote-trading or pork barrelling is not only acceptable but probably an inherent part of the political system, but is probably rejected as immoral by many voters. Secondly, under majority rule it is possible for a politician to attain and retain office by persistently adopting policies that involve the coercion of one or more minority groups by the majority.[4] This may be unacceptable, even to some members of the majority group, perhaps because they realize that persistent discrimination against minorities can lead to revolution or secession, which would not be in the interest of the majority. The mystique that politicians serve 'the public interest' rather than their own may be an ideological solution to the dangers inherent in the adoption of majority rather than unanimity rule.

While concern about the coercion of minorities is undoubtedly warranted, some of the public's views of politicians and politics are dangerously romantic. When martyrdom is the ostensible norm, most will be found wanting! Moreover, could a political system long survive a succession of heroes who acted without regard to the personal costs of their behaviour? Would it not be dangerously un-

3 Neither Downs nor Breton take this competition among members of the same party into account.

4 The word 'coercion' is used in the Breton sense of making the minority worse off. An example of such a tactic would be a government overtaxing a resource peculiar to a region in order to subsidize other regions. If the number of seats in the overtaxed region were sufficiently small, the residents of the region could be written off politically if the support gained elsewhere because of the subsidies was sufficiently great.

stable? Presumably what is required is not a succession of saints but sets of rules that provide the incentives needed to direct the behaviour of self-seeking politicians in the direction that protects the interests of the weakest.

Let us now attempt to state the derivative rules that politicians follow if they are to pursue their own interest as previously defined. The list does not purport to be comprehensive.

Intra-party rules

1 There is nothing for nothing; a favour received is an obligation incurred. Failure to meet obligations results in punishment.

2 When there is a conflict between the interest of the candidate and the interest of the party the candidate usually must choose the latter course after extracting the best possible price – an obligation from someone else in the party.

3 Advance within the party is dependent upon: capacity to be elected in one's own riding; perceived possession of representational characteristics (e.g. regional, industrial, cultural) that help to deliver the vote in other ridings where these characteristics are valued; alliances with other members of own party, pressure group leaders, and journalists; capacity to function effectively in the House; capacity to administer a department (e.g. not embarrass the party); and capacity for policy innovations.

Anything the elected member can do to further the appearance of the possession of these kinds of attributes should be looked upon as an investment. They are listed in the approximate order of their relative importance.

Ministerial-bureaucratic rules

1 With rare exceptions, career bureaucrats are not committed to particular parties or ministers but to the maintenance and strengthening of the bureaucracy and of their positions within it. Ministers who support their senior officials within the bureaucratic system can expect bureaucratic support in the political system, and conversely. This means, in effect, that ministers must accept the incentive system within which the bureaucrat works and not demand that he behave in ways that would damage his current or potential position in the bureaucracy.

2 Many senior bureaucrats have about as much power to reward and punish ministers as ministers have to reward and punish senior officials. Successful senior officials have a complex and extensive network of alliances: within the bureaucracy, with other ministers, with the prime minister (or members of his immediate staff), with journalists, and with interest group leaders. They can therefore conjure up or suppress information and support. They can also delay or expedite.

3 From time to time a minister can get rid of a senior bureaucrat. But this is relatively rare because the prime minister, who is responsible for these appoint-

ments, almost invariably has to find some other post for the official that is roughly comparable, at least in aggregate benefits (e.g. less prestige but more perquisites). These kinds of posts are always in scarce supply relative to the demand for them. The need to find a safe haven for the discarded bureaucrat probably arises from the pressures from other senior bureaucrats who find it in their interest to protect one of their own. Who knows who might be next?

Ministerial-interest group leader rules

1 Professional interest group leaders have to appear to be able to deliver something of value to those they represent and therefore have to be able to deliver or withhold something of value to ministers in order to be able to bargain effectively.

2 The best of them probably have as good an understanding of the rules governing the decision-making system as those with whom they deal: politicians, bureaucrats, journalists, and their own members. This gives them a great advantage because they know precisely where, when, and how to apply pressure. They are, in a sense, mercenaries: guns for hire. They gain bargaining power with ministers by the following strategies: creating obligations by providing information, campaign contributions, favourable publicity, food, drink and travel; threatening the imposition of costs by withdrawal of any of the foregoing, or marshalling public criticism of policies or personalities.

3 Ultimately, of course, interest group leaders seek to deliver decisions favourable to those they represent. However, all sides recognize that this may be impossible. They are judged, at least by the more sophisticated, in terms of how well they did relative to the difficulty of the task. Obtaining access to a minister for a delegation may be a major accomplishment, even though no direct result is apparently obtained.

4 Professional interest group leaders can incur obligations to ministers when the latter act in such a way as to protect the former from their own extreme supporters by making them *seem* effective.

Ministerial-media rules

1 Journalists and professional interest group leaders are similar in several respects. Both are intermediaries. Journalists need news. In order to obtain it they usually have to offer something in exchange. That something can be positive or negative: they can offer support for a politician, a party, or a program, or they can threaten disclosure of embarrassing information.

2 Journalists have even shorter time horizons than politicians. They need a story every hour, every day, every week, or every month, depending upon their medium. This makes them appear more unscrupulous, for the costs of betrayal are

distant, while the payoffs from a 'scoop' are immediate. It also makes most of them unable to invest in the acquisition of detailed knowledge about technical subjects. The result is that sensational trivia have enormous importance for the politician. Ideas that cannot be explained simply and briefly are virtually valueless. Favours given in complex legislation are rarely discerned.

THE RULES AND CONDITIONS OF THE BUREAUCRATIC GAME

1 Senior bureaucrats, like politicians, sacrifice money income for perquisites, pride, and prestige. However, unlike politicians, bureaucrats generally settle for less of those benefits in exchange for much greater security of tenure.

2 The most senior bureaucrats have career alternatives outside the public service because they have knowledge of how the system works, access to other bureaucrats and politicians, and a public image. Generally speaking, however, these alternatives are treated as fallback positions. Relatively few bureaucrats enter the public service with the intention of obtaining qualifications or influence that they can subsequently sell.

3 Most senior public servants try to maintain and strengthen the power and influence of the public service as a whole. This arises because protecting 'the system' protects their own positions; they naturally believe that the system that elevated them to the top cannot lack virtue; and they are frightened by the retaliatory action of other public servants if they appear to be disloyal to the system.

4 Senior bureaucrats are, in a sense, friendly adversaries. They compete for budgets, personnel, ministerial time, and appointments to offices of greater prestige. But they are friendly in the sense that they recognize the rules of the game that require that senior public servants not compete with one another at the expense of the system as a whole. Winning at the expense of the system is punished by other public servants.

5 Senior public servants punish other senior public servants by advising a minister to fight the proposals of the enemy's minister, withholding information, enticing away the enemy's staff, withholding favours from the enemy (e.g. accommodation), and social ostracism.

6 Senior public servants do not have the power to fire subordinates, except under the most extreme circumstances. They have only limited scope for rewarding them through salary increases or other perquisites. Their main power lies in their ability to affect the rate of promotion. Those who are not anxious for promotion are almost impregnable. Zealots, those who pursue a course of action without regard to its affect on their careers, are a serious potential threat to the system and are rarely given positions of authority.

7 Those senior public servants whose role is largely advisory, as distinct from administrative, usually cannot communicate to their subordinates the 'real' nature of the problems with which they are grappling. This is partly because of a shortage of time and partly because the issues or strategies are considered to be too sensitive. Consequently their subordinates are often underworked or working on questions that no one is asking. This means that despite the large staffs supposedly supporting them, most senior public servants playing advisory roles are, strangely enough, playing by ear a large part of the time.
8 Senior officials who press for greater efficiency in their own departments are likely to be hurt because: ministers object to the public outcry from releasing redundant employees or from cancelling contracts with suppliers; subordinates retaliate by doing less work or poorer work while not giving grounds for dismissal or even grounds for denial of salary increases or promotions; tight organizations are hurt most when across-the-board stringency is applied; the 'savings' are not available to the senior official - they are appropriated by other departments or by the taxpayer; senior officials who are good administrators have less prestige than those perceived to be influential policy advisors, so that the time devoted to administration is at the expense of time devoted to the more prestigious function; hard information is not available on which to assess efficiency, so that the tough senior officials appear arbitrary; deputy heads who are perceived to be arbitrary find it more difficult to attract and retain competent subordinates.
9 Because of the short time-horizon of ministers - they require a payoff before the next election - senior public servants are sorely tempted to propose short-term solutions to long-term problems. The public servant who is successful in devising and selling a facile 'solution' will strive to move to another post before the limitations of his solution become obvious. If this stratagem works, the failure will appear to be the incompetence of his successor.
10 Senior officials seek to gain monopoly positions to increase their prestige (perceived power or influence). They strive to acquire exclusive jurisdictions over the provision of advice to superiors, control of access to information by superiors, and the provision of an essential service (e.g. accommodation or recruitment). Three arguments are usually advanced for stronger monopoly positions: avoidance of duplication, the need for confidentiality, and the lack of accountability associated with shared responsibility. Monopoly positions are constantly under attack, however, by other senior officials, who of course do not wish to be indebted to a colleague.
11 Senior officials seek desperately to avoid losing the 'right' to participate in the consideration of a problem. Capturing an interest in a problem is at least as important as finding a resolution to it, because influence, budgets, and staff often follow the allocation of responsibility for dealing with a problem.

THE RULES AND CONDITIONS OF THE GAMES PLAYED BY INTEREST GROUP LEADERS AND THE MEDIA

It is not necessary to discuss the rules and conditions that apply to these groups in detail because they can be inferred readily from what has been said.

Professional interest group leaders have to appear to be unconditionally committed to the interests they represent and as capable of influencing government decisions as their rivals. Perhaps of greater importance is the fact that maintaining the membership of such groups is precarious, because membership costs are tangible and immediate, while the benefits are often intangible and distant. There is also the ever-present difficulty that, because members rarely perceive that they have identical interests, the internal competition for control, perpetual threats of secession, and the problems of appearing to present a united front, absorb much of the professional leader's energies. This means that except when the group is small or the threat to the member's interests immediate and dramatic, or when the association offers some side benefits, interest group leaders are often not effective bargainers either with politicians or the bureaucracy. Many of their demands are more ritualistic than real: witness the annual presentations of the Canadian Labour Congress and Canadian Manufacturers' Association.

Journalists work for companies whose profits depend upon advertising revenues, which in turn depend upon their coverage (paid circulation or number of listeners or viewers). The owners therefore reward journalists in accordance with their success as measured by this criterion. The rewards take the form of prestige (bylines), money, and perquisites (travel and expense accounts). Because the public wants to minimize the costs of obtaining information, the most successful journalist is likely to be one who simplifies, condenses, and uncovers issues that are sensational but not necessarily significant.

The journalist obviously wants to obtain information at the lowest possible cost to himself. Those who possess information are only likely to provide it in a kind of exchange relationship. The journalist may be able to obtain information by threatening to impose costs on those who do not co-operate. Politicians and bureaucrats are therefore at great pains not to make 'mistakes' that could be converted into sensational issues or used as leverage to obtain other information.

The best journalists often discern internal conflicts within the several games and take advantage of the hostilities among the competitors to obtain information which is provided not to help the journalist but to hurt an enemy on the same team.

PLAY-OFFS AMONG THE GAMES

While they are undoubtedly improvised and incomplete, we have now stated what appear to be the most important rules under which the four types of games are played and some of the inter-relationships among them. In this brief section an attempt is made to examine these inter-relationships more closely.

All games are related to all other games all the time. But because the expenditure budget is an annual event (although *Supplementary Estimates* make timing less rigid than this statement would suggest) it is perhaps useful to think of the decisions embodied in it as the results of an annual playoff series among the four types of players. The issue is not, of course, the terminology but rather obtaining some understanding of what goes on.

The first and foremost point that must be made is that while the players *within* each of the political and bureaucratic games are interdependent, equally important is the fact that *all* of the games are interdependent. These intergame interdependencies are extremely complex. As indicated above, politicians need bureaucrats and vice-versa; the media need the news generated by politicians; politicians need favourable publicity; special interest groups need political concessions; politicians need electoral support and campaign funds from special interest groups; bureaucrats need special interest groups as sources of information and for the pressure they can bring to bear for departmental initiatives; special interest groups need bureaucrats to keep them informed as to how best to exert their pressure, and so on.

These interactions usually take the form of some kind of exchange: 'If you do this for me, I'll do that for you.' Seldom, of course, are these exchanges so explicit or so simple. A tacit understanding that a favour accepted is an obligation incurred is more likely to exist than even a verbal agreement. Furthermore, some of the exchanges are essentially implicit blackmail. It is understood by both parties that if a favour is not granted punishment will be inflicted – whether in the form of lack of support for a proposal, or disclosure of embarrassing information, or a forthcoming promotion frustrated. The winners in each of the games are, almost by definition, most adept at getting the most favourable terms in these exchanges. They first of all acquire something the players in other games want (including information others do not want disclosed) and then through their bargaining skills exchange it for something they want even more themselves – all within the rules of propriety in most cases (at least the rules of propriety prevailing in their own game, if not those of society in general).

The second point is that this search for chips with which to bargain, and the bargaining itself, are continuous, occurring among all the games simultaneously. The players may change (and of course they do, through elections, recruitment, promotion, retirements, etc.) but the games go on.

The third point is that the budget is almost unique (an election has the same characteristics and more!) in that this bargaining among the players in the various games is, to a considerable extent resolved at a point in time. The *Estimates* must be tabled. As indicated above, there are, of course, the *Supplementary Estimates.* The losers (or at least the disappointed) *may* have another opportunity to press their case during the coming fiscal year. And there is always next year. But a year can appear to be a long time to the players. Obtaining funds through a *Supplementary Estimate* is at best uncertain and usually requires extensive negotiations and probably also surrendering some carefully garnered chips or incurring heavy obligations. The expenditure budgetary process has therefore a kind of frenzy and desperation about it that reaches a crescendo when the final hard decisions are locked in for the year. The winners - politicians–bureaucrats–interest group leaders - congratulate themselves (often mutually) on how well they bargained; the losers try to console themselves with the thought that they did not have as many chips with which to play. The losers also begin to put together excuses for the members of their own constituencies and wonder about the likely impact on their future careers.

The next section seeks to elaborate upon the expenditure budgetary process using this framework.

THE BUDGETARY PROCESS: ONE OF THE PERPETUAL PLAYOFFS

The budgetary process would be incredibly different than it is if the assumptions of some public finance theorists held true, that is, that transactions costs (e.g. information, negotiating, and enforcement costs) were zero and a unanimity voting rule prevailed. Voters would have arrayed before them, on a continuing basis, packages consisting of all possible combinations of tax-expenditure changes. Each individual would be fully aware of the potential 'real' impact of each package on himself and everyone else. The head of state (presumably elected unanimously) could know, at any point in time, not only which packages could be ruled out of court because they were unacceptable to one or more persons but also which of the infinite number of remaining alternative packages was unanimously accepted as the best package. There would be no losers. Government would be a relatively simple matter of implementation.

The farfetched notions of zero transactions costs and the rule of unanimity in collective decision-making do serve a useful purpose in helping us to understand the existing process. Nevertheless, the fact that there are heavy transaction costs and the fact that there is majority rather than unanimity rule together explain much of what actually goes on.

Consider first a hypothetical world where information costs were zero but the majority rule rather than the unanimity rule prevailed. The voters would have arrayed before them, as before, packages consisting of all possible combinations of tax-expenditure changes. They would know with certainty their effects. However, with majority rule, the head of state (who conceivably might not be the choice of 49 per cent of the voters)[5] could select any package that satisfied at least half of the voters and remain in office. One-half of the voters could perpetually coerce the other half. That is to say, a majority could continue to adopt legislation that benefited themselves at the expense of the minority.

When information is not costless – indeed much information is not attainable at any price – the plot thickens. It is not possible for anyone, much less the whole electorate, to consider all possible tax-expenditure change packages because there are an infinite number of conceivable ones. It is not possible for individuals to determine unequivocally all of the effects of a particular package of policy changes on themselves or on others. The head of state cannot know the 'true' preferences of the electorate, and certainly not continuously! Groups of voters must be represented by other individuals who are not the choice of many whom they represent. These representatives must seek to divine how their constituents will *perceive* the impact of particular policy changes and how these perceptions will be translated into votes at the end of a period of time of uncertain length that will have encompassed a vast number of policy changes. Furthermore, in order to get the legislation passed that he wants, presumably because he believes it will help him get re-elected, the representative often must agree to support the legislation of other representatives that he does not want in exchange for their support – always wondering if he has paid too high a price!

Political institutions in general, and the budgetary process in particular, can be looked upon as the means that have slowly evolved of coping with two inescapable aspects of the human condition: limited knowledge, time, and effort; and the fact that many of the interests of individuals are in direct conflict, in the sense that most individuals most of the time seek to increase their own utility even if this means forcing a reduction in the utility of other individuals. Politics is a way of producing, in a reasonably orderly and timely manner, decisions that necessarily involve conflicts among individuals and groups of individuals in the face of differences of opinion about standards and facts that can never be completely resolved.

This is not to say that any budgetary process that grinds out decisions is as good as any other. The organizational structure within which it takes place, the

5 Indeed, when the numbers of voters in each riding are disparate, the percentage could be considerably less than 49 per cent! With three or more candidates, less than 49 per cent can suffice in a riding, of course.

procedures adopted, the quantity and quality of information available, the characteristics of the individuals involved, all presumably have an impact on the decisions produced. It is perfectly legitimate for those who do not like the decisions to propose changes in these determinants. But it is vitally important to recognize two points. First, it is difficult to imagine any significant change in the process that would not be perceived by some individuals (either actors in the present process or recipients of benefits under it) as likely to make them worse off. Unless they were compensated in some way, they would resist it. Second, there can be no technical, once-and-for-all solution, any more than there can be simple technical solutions to the problems of judging the guilt or innocence of men standing trial in a court where there are inescapable conflicts about the meaning of the law or the facts.

THE BASIC FEATURES OF TRADITIONAL BUDGETING

Traditional budgeting under the parliamentary system often works in this manner: the same individual is both minister of finance and chairman of the committee of cabinet known as the Treasury Board.[6] In the former capacity, he is responsible for recommending the level and sources of revenues for the coming year. In the latter capacity he is responsible for preparing the *Estimates* for submission to the legislature and controlling the expenditure of monies subsequently voted by the legislature. Other ministers are responsible for submitting the expenditure proposals of their departments. The minister of finance has a staff to assist him that is small relative to the staffs of departments who are preparing their budget proposals. His staff necessarily lacks expertise in all of the technical operations of all the departments. Departmental proposals are on an input basis, with little if any indication of the kinds (much less quantities or qualities) of outputs they would produce. They do not differentiate, except nominally, between the funds required to maintain existing activities and the funds requested for the enrichment of old activities. The prime minister, or the cabinet as a whole, has given, or is alleged to have given, a degree of commitment to at least some of the additional expenditures. No attempt is made to set forth the costs of adopting new initiatives beyond the current year or the current year plus one. All departmental proposals arrive on the desks of Treasury Board officials at one time with a tight deadline for completing the *Estimates* because of legislative requirements.

6 In Canada, the two functions were placed under different ministers following the recommendations of the Glasscoe Commission.

The players

Some of the gamesmanship aspects of this kind of process are immediately apparent. Because the minister of finance takes more of the blame for tax increases than his colleagues, he is more inclined than they are to push for expenditure restraint. The revenue 'pie,' as determined by the minister of finance, is almost invariably smaller than the collective demands of other ministers. They are, perforce, competitors. For three reasons it is in the interest of ministers (other than the minister of finance) to obtain the largest possible increase in the budgets of the departments for which they are responsible. The announcement by the minister of new or enriched programs helps his own prestige and hence the likelihood of his personal re-election. This increases his bargaining power within the party and with the prime minister. Furthermore, large budgets make it possible for the minister to reward his own officials through more rapid promotions and thereby gain their support.

Treasury Board officials are adversaries of departmental officials because cuts have to be made somewhere and the departmental officials do not want to provide the information on the basis of which the cuts could be 'justified.' The minister responsible for a particular department is often in an adversary relationship with the deputy head because the latter pushes proposals the minister believes cannot be sold and the minister wants 'better' proposals that would be more salable. Similar conflicts exist between the deputy head and his subordinates, who are also competitors since the deputy head cannot put forward all their proposals because the total would be unreasonable. An adversarial relationship usually exists between particular ministers and the pressure groups they represent, who believe that their interests are not being pushed hard enough.

Three factors help to keep the degree of conflict within bounds and produce a resolution. The ministry as a whole will be judged on the basis of the total policy package that must be publicly supported by all ministers. It is in the interest of each minister to be a member of a team that produces a 'balanced' package of additional expenditures with 'acceptable' tax changes. Herein lies the power of the minister of finance. The prime minister has the last word in principle, and usually great influence in fact, in resolving conflicts. This power arises in part because of his control over portfolios and in part because of his control over party financial support in elections. Finally, the battle cannot go on forever; the *Estimates* must be tabled and there are other calls on the time of the participants.

Procedures

Procedures themselves can affect the outcome of the process. Some of the more important alternatives are best illuminated by the following questions.

- Are accurate records of cabinet decisions kept so that the extent of prior commitments can be ascertained? Who has access to this information?
- Is cabinet discussion of the policy proposals of particular ministers based on written submissions? What do they contain? To whom are they circulated? How much time is available to analyse them and prepare comments and arrange alliances?
- Who controls the agenda for cabinet meetings?
- What is the elapsed time between the submission of departmental budgetary proposals and the tabling of the *Estimates*?
- What access do Treasury Board officials have to departmental information before and after their submissions?
- When does the minister of finance inform his colleagues as to the revenues that will be available for the coming fiscal year relative to the date on which departmental budgetary submissions are required?
- Do Treasury Board officials advise departmental officials on their recommendations before they are reviewed by the minister of finance or by the Treasury Board?[7]
- How much time does the Treasury Board spend reviewing departmental proposals and the recommendations of its staff?
- Do ministers of particular departments have an opportunity to present these cases to the Treasury Board? Or is their only appeal in cabinet?
- What legislative procedures exist for the examination of the *Estimates* by the opposition?
- Do the rules and procedures controlling departmental expenditures of voted funds make it possible for the Treasury Board, or its officials, to block or delay expenditures they were unable to block at the *Estimates* stage?
- What are the powers of the auditor appointed by the legislature?

These and similar procedures constitute the rules within which the budgetary game is played. Rule changes not only call for changes in strategies and tactics but almost always help some of the adversaries relative to others. Battles over the procedures are therefore extremely intense and frequent.

Information

Of vital importance in the budgetary process is the quantity, quality, accessibility, and timing of information, the currency of the senior bureaucracy. Influence is not possible unless the individual has access both to sources of information and to the attention of decision-makers who base their decisions, at least in

7 Secret criticisms are difficult to refute.

part, on it. Freely available information naturally does not afford those who possess it any advantage. Therefore, influence is maximized by obtaining exclusive access to sources of confidential information and by securing the position of exclusive supplier of it to those who make policy. Information is carefully guarded. Those who possess information are only willing to trade it for a quid pro quo.

While it is impossible to document, the author asserts that the traditional budgetary process is carried out with surprisingly little 'hard' information other than the dollar figures themselves, which on analysis turn out to be based on soft information. Cabinet policy decisions are usually based either on no documentation or on documentation of a persuasive and rhetorical rather than analytical nature. This is not surprising, given that it is an adversarial situation. Here too, proof is impossible because of secrecy provisions.

Departments often do not collect data that would allow assessments of the efficiency of their operations, much less the cost effectiveness of their programs (even in the limited cases where this is feasible). There are, however, four special circumstances where these data may become available: when departmental officials are firmly convinced they have an overwhelming case for more resources and believe they have nothing to lose; when departmental officials are searching for persuasive evidence and feel confident they can suppress or discredit unfavourable findings; when particular officials believe that more information would further their own careers (the image of the knowledgeable or the efficient administrator); and when legislative requirements exist that require the collection and disclosure of information.

The reluctance to collect and analyse information at the departmental level usually arises because additional funds have been forthcoming without it (why tamper with a successful formula?), because of conflicts within departments between those staff officers who want more information and the line officers who resist providing it because it would reduce their monopoly power or increase the extent to which they could be rewarded in accordance with their performances, and because there is a danger that unfavourable information would get into the hands of adversaries.

The prime minister, the minister of finance, the chairman of the Treasury Board, and the cabinet as a whole, are seemingly unwilling to demand, or at least unable to secure, more and better information from departments for a complex set of reasons. Ministers responsible for individual departments are treated as though they are responsible! To demand more information from a particular minister would be to suggest a lack of confidence in him. To demand more information from all departments simultaneously and continuously would be to create an avalanche of paper containing much information that was irrelevant or indigestible. Given the short time horizons of ministers, and the fact that a great

deal of their attention is devoted to responding to immediate crises, information needs are frequently not forecast and therefore cannot be met before a decision has to be reached. Experience suggests that attempts to obtain relevant and timely information from a reluctant supplier are often abortive. Delay is easy, and a decision, once reached, is usually impossible to reverse - even if the information, when it finally arrives, indicates a different course of action.

Perhaps more fundamental, however, is the possibility that better information could impede the decision-making process. Compromises have to be reached. It is sometimes easier to swallow an unpalatable decision without *explicit* knowledge of all of the consequences. Decisions based on ignorance do not raise so many questions of personal integrity or collective responsibility - particularly when there is vote-trading or pork barrelling involved. Moreover, there is a fear among ministers, which probably has some validity, that heavy reliance on 'hard' information might deaden the sensitivity of their antennae, their 'feel' of the changing attitudes of the electorate, might make them more captive of the technical adviser, who may be incompetent or self-seeking or both. Last, but not least, it must be recognized that a government's decisions do not have to be better informed than the opposition or the public that assesses them.

The failure of the officials of the central agencies (e.g. the Prime Minister's Office, Cabinet Office, Department of Finance, and the Treasury Board) to demand or secure better information from operating departments or to generate it themselves is basically a reflection of the factors already discussed: their own ministers are reluctant to press for information which departmental ministers and their officials are reluctant to supply. However, of all the participants in the budgetary process, central agency officials have the greatest interest in improving the quality of available information, partly because they have, or think they have, a clearer perception of the 'errors' that arise in its absence, and partly because it would give them more power and control.

It perhaps should be pointed out that, in the absence of power to obtain departmental information, the officials of the central agencies have to make implicit deals with departmental officials in which departmental information is exchanged for other favours. It is no accident that PPB, benefit-cost analysis, 'management by objectives,' and performance measurement systems were developed and pushed by staff officers, particularly those in central agencies. These techniques were looked upon by the latter as a way of gaining leverage in the battle to obtain more and better information.

Staff advisers

Changes in the number and quality of the senior staff officers of the central agencies and of operating departments are an important part of the adversary

process. When a particular department obtains more and better economists, lawyers, financial advisers, and so on, it threatens its competitors. More and better memoranda, more meetings, and tougher negotiations can be expected. The adversaries therefore strive for more senior staff officers of higher quality – where quality is defined in terms of a capacity either to produce ammunition for the interdepartmental war or to fight in the trenches of the interdepartmental committee where negotiations are actually carried out.

To the extent that this upgrading in the number and quality of staff officers is in lock-step across departments, the results are relatively small because they tend to cancel one another out. The more informed argument is met by the more informed rebuttal. The information going to ministers becomes more subtle, technical, and voluminous, but not necessarily more helpful. The obvious question to ask is how information could be improved. But this immediately raises the question From what point of view?

To tackle the last question first: it seems that, from the point of view of the cabinet as a collectivity, what is needed is better information with which to assess the impact of policy proposals in general, and budgetary proposals in particular, on the outcome of future elections. As mentioned above, there is a strange reluctance of politicians to admit, and of officials to acknowledge, that most policies most of the time are based on ministerial perceptions of their likely direct or indirect electoral impact. The more successful senior public servants are undoubtedly well aware of this precept and act accordingly. However, staff members 'at the working level,' to use a common but somewhat ironic phrase, frequently act as though they were serving a congregation of individuals seeking martyrdom. This strange insensitivity of many staff officers to the interests of ministers probably arises in part because of a confusion between the sound idea that bureaucrats should not act in such a way as to make themselves unacceptable to the other party if it were elected to office and the silly idea that information that would be useful in making political decisions is in some way tainted. One is tempted to say about the prevailing attitudes of many junior advisers that they are truly non-partisan inasmuch as they stand ready to be equally ineffective for any political party.

Another part of the explanation of political insensitivity by bureaucrats probably arises because of the training of some kinds of officials. Lawyers, because they are trained in the virtues and practices of the adversary process, are often superior advisers. They may not know much about the subject matter but they rarely get confused about the nature of the game. Economists on the other hand often know more than anyone wants to know about the subject matter, but they forget, if they ever understood, the basis of the games being played.

It would take a book – or a shelf of books – to elaborate on the theme of the kinds of information that politicians would find useful but often do not obtain

from their advisers. Perhaps three words best convey the heart of the matter: disaggregation, attitudes, and perceptions. Ministers would benefit enormously from more information on the estimated effects of policies on specific groups of individuals. Who gains? Who loses? By how much? They would also benefit from more information about voter attitudes, again on a disaggregated basis. Finally, they would benefit, in the sense of saving valuable time, if analysts were to recognize the symbolic importance of many government acts. Ministers are elected on the basis of the *perceptions* of voters, not on some kind of 'reality' that is real only to the analyst.

There is, however, another side to this basic proposition. While ministers could be better served by their advisers, much more important is the paucity of information available to the public. Decision-makers do not have to be better informed than the public they serve or their competitors. Unless and until the opposition and the public have more information with which to assess the impacts of existing policies or policy proposals there is little likelihood that the quality of information inside the system will be substantially improved. When ill-informed decisions meet with electoral success, why bother to get more information?

The problem is, of course, that informing the public so that it becomes more demanding requires access to information that it is not in the interest of the government of the day, or of the bureaucracy, to disclose. Those interest groups who perceive that they are 'winning' under current policies and processes are not motivated to press for change. The 'losers' often do not know what information to ask for, or can be brushed off with the statement that a report was prepared for the advice of ministers and is hence 'confidential.' It is not in the interest of most voters to make the investment necessary to determine precisely the extent to which particular programs serve their interest! Journalists have little incentive to do the time-consuming work necessary to be able to ask the right questions, much less to try to find the answers to them.

The situation is equally depressing in so far as academics are concerned. They have little incentive to undertake the analysis of actual programs because the conceptual problems are messy and the data are not readily available. Ringing elegant changes within a well-established framework has a greater personal pay-off per unit of effort, generally speaking.

THE EXPENDITURE BUDGET AND THE VOTER

This section attempts to set forth the basic, purely political rules of expenditure budgeting. That is to say, it addresses the question: What rules do ministers follow in order to maximize the likelihood of their re-election? It draws heavily on the analysis of the determinants of voting behaviour discussed in chapter 2.

Each jurisdiction is divided into a number of ridings and in each riding there are a number of qualified voters. Under a two-party system, which we are assuming to exist to avoid the complexities of coalitions, these voters can adopt one of four alternative decision rules (we ignore here the interest group activities of some individuals that were discussed earlier): the indifferent voter will abstain from voting because it will make no difference to his future well-being; the committed voter will vote for a particular party label; the uncommitted voter will vote for the party perceived to be the lesser of two evils; the marginal voter will abstain from voting except when he perceives that a few more votes for the party that is the lesser of two evils could affect the outcome.

It should be noted that these rules are ordered to reflect the fact that the quantity of information required to pursue them rationally increases progressively as one moves down the list. An indifferent voter does not have to read a newspaper or follow a news broadcast. A marginal voter has to follow political events closely not only to determine which party is likely to serve his interest best but also to assess voter opinion. One has the impression that these costs are more burdensome for uneducated or unintelligent voters, so that they are more likely to adopt one or the other of the first two rules. But perhaps the ignorant and the stupid do not know what they do not know!

It should also be noted that the choice of a voting decision rule probably hinges on the nature of the individual's interest. Persistently persecuted or favoured minorities are likely to be indifferent to elections, for they realize that they are almost certain to get the same treatment whichever party is elected. Voters who strongly identify with a particular ethnic-linguistic-religious-class group ('our interests versus their interests') are likely to adopt the committed-voter decision rule because of some real or imagined historic cost or benefit for the group associated with one of the parties. Those who perceive that they have diverse or vulnerable interests and who are intelligent or educated enough to handle the information requirements at reasonable cost are unlikely to adopt either of the first two decision rules. No doubt there are also other factors leading voters to adopt a particular decision rule.

When the proportion of the voters in a riding who are either uncommitted or marginal is large enough that their votes are decisive, we can refer to the riding as a swing riding and to these voters as swing voters. To remain in office the majority party must continue to appeal to such swing voters as the lesser of the two evils *and* must also create the impression that the outcome is likely dependent on a few votes one way or another in order to activate the marginal voter.[8]

8 Downs does not appear to distinguish the marginal voter in the marginal riding (Congressional District). Rather he seems to think solely of obtaining a clear majority. Perhaps this reflects the differences between the parliamentary and congressional systems, primarily.

One voting strategy under a two-party system is sufficiently important to warrant special mention – the protest vote. Even though an uncommitted voter may prefer party A to party B, if the voter thinks that party A is going to be elected however he votes, he may decide to vote for party B in an attempt to induce party A to serve his interest even better in the future. If, as one would suspect because of the decision rule they have adopted, uncommitted voters are poor forecasters of the voting behaviour of others as compared with marginal voters, they may unwittingly overturn the majority party. This is another reason why the majority party must somehow create the impression that the outcome of each election is in doubt.

While there are other more dramatic strategies, most of the time the majority party will seek to achieve two things to remain in office. First, it will try to retain the support of its committed supporters by *appearing* to them to be likely to continue to serve their interests better, or hurt them less, than the opposition party. Because those who adopt this decision rule have opted to minimize their information costs it is possible to hurt their interests materially without triggering a reconsideration of their attachment to the label. Second, the majority party will try to hold the support of enough swing voters by *appearing* to them to be likely to deliver at least as many benefits or to impose at least no more costs than the opposition party, and to have lost some support since the last election so that every vote will count next time; but it must also avoid appearing to have lost so much support that a vote for the party is likely to be wasted.

Obviously this is an extremely difficult feat. It is not simply a matter of 'giving the voters what they want,' for this is an impossible task. Wants are inconsistent among interest groups, changeable, and apparently ever expanding. Nor is trying to 'give them what they want' even necessary, for if the opposition party can be discredited as incapable of delivering as many benefits or more likely to impose larger costs, little need be done to remain in office.

Timing is of crucial importance. Costs should be either imposed as far in advance of an election as possible, so that they are capitalized and forgotten, or postponed for such a long period that their present value is low (borrowing). The converse is true of benefits. The longer an inadequate program is in effect the more likely that its inadequacies will become obvious. On the other hand, there are usually administrative or technical weaknesses in new programs that cause discontent at the outset. Complex programs introduced just prior to an election can therefore be a source of embarrassment, for the critics can blow up the short-term inadequacies to the point where the long-term benefits are overshadowed within the electoral time-horizon.

The longer the majority party is in office the more its promises become a debased currency. If a government has been in office for a term or two, and has not dealt with a problem that has been generally recognized throughout the

period, its promises to act after the next election are hardly credible. This is one of the few advantages possessed by a minority party – it does not have to live with its record! On the other hand, there is usually a reason why a majority party has not acted to 'solve' an apparent problem, particularly if it has promised to do something about it. More often than not the majority party has found that any known 'solution' would create more political costs than the political benefits it would bear. The opposition must phrase its promise in such a way as not to alert the losers unless they have done their political arithmetic carefully!

We emphasized the importance of perceptions in describing the task faced by the majority party. Voters are won and lost on the basis of perceptions of reality, not on the basis of what is 'really happening' – which cannot be known in any event because everyone has perceptual limitations and the measuring instruments are imperfect. Public perceptions can be manipulated in a host of ways. Some of the more obvious are: withholding information from the public on a highly selective basis, so that what is said is not false but does not convey a true impression; burying an important cost in a large package of fluffy benefits; burying unpopular changes in a maze of technicalities; distracting attention by releasing sensational but trivial information at the same time as important, unpopular information is made public; buying off the critics indirectly if not directly.

From what has been said the budgeting decision rules of the majority party are therefore straightforward. First, the benefits (increases in the subjective net worth of voters) are to be made as politically efficient as possible, in the following ways.

- minimize the benefits provided to those whose support is assured or hopeless;
- adopt benefits provided either by regulation (e.g. granting monopoly power) or by tax concessions, which are doubly valuable because on the one hand the costs are hidden to the non-beneficiaries and on the other the beneficiaries neither lose face nor are constantly confronted with legislative review;
- adopt symbolic benefits (benefits inadequate relative to the magnitude of the problem on the basis of objective analysis) that show the appropriate degree of concern, such tokens being often as valuable in political terms as 'real' benefits that are much more costly in budgetary terms;
- do not give to small interest groups benefits perceived by non-beneficiaries to be so generous that jealousy is aroused;
- do not give tangible benefits that are so small that those who receive them are either unaware of their good fortune or, what is worse, insulted;
- do not give benefits so far in advance of an election that they will be forgotten;
- because most voters are unable to determine the indirect impact of government policies with any certainty, adopt programs that can be credited with

accomplishing favourable outcomes that would likely have happened in any event (but beware of being blamed for unfavourable outcomes that were not the result of government policies);
- ensure that your principal advisers are sufficient in number and quality that there is always a range of proposals on the table (or in the filing cabinet) that could be adopted to serve the interest of each significant group of swing voters if this were necessary;
- engender enough competition among advisers that they disclose the weaknesses in each other's proposals.

Second, minimize the political costs (decreases in the subjective net worth of voters that lead them to vote against the majority party or organize opposition to it) of financing these benefits:
- tax, in one way or another, committed supporters and committed enemies in order to be able to provide net benefits to swing voters;
- spread the costs as widely and gradually as possible so that the increased burden is barely perceptible, easily forgotten, and too small to warrant mounting an organized attack;
- obtain the maximum increase in funds by means of transfers (in fact if not in form) from other governments, because such revenues are politically costless;
- shift the blame for increased taxes on to the other levels of government for not meeting their responsibilities or for exceeding their powers;
- borrow to the limit, short of pre-empting through higher debt charges future expenditure increases in the ministry's time frame (or, in the federal government, generating inflation at a higher rate than other nations);
- earmark new taxes for purposes that are difficult to attack;
- where possible label the tax as a fee, contribution, or premium, which entitles those who pay it to a specific benefit that is not available to those who do not 'pay';
- tax 'sin' with impunity up to the point where the costs of policing exceed the extra revenues;
- collect the tax in such a way that the average voter is not constantly reminded of what he is paying, avoiding in particular any collection method that requires the taxpayer to write a larger cheque payable to the government (e.g. property taxes);
- exercise great caution in implementing tax changes to correct significant 'inequities,' for the additional burden is, almost by definition, confined to a relatively small group, the members of which can, in personal cost/benefit terms, readily justify mounting a major defence campaign;
- exercise the greatest caution of all in cutting existing programs in order to free funds for new programs (or, if one can imagine it, permit tax reduction!) because

three groups are alienated simultaneously: the beneficiaries of the program, the bureaucracy in whole or in part, and the private sector suppliers who provide some of the inputs under contract;
- the more vague the threat or opportunity the better, because this makes it more difficult for voters to compare actual costs of programs with potential benefits (e.g. threats to security or payoffs from medical research). These kinds of programs make it possible to provide large benefits to suppliers at relatively low political cost.

IMPLICATIONS

Let us now recapitulate the argument of this chapter and highlight the major implications. Three factors seem to be of particular importance to the expenditure budgetary process: the four distinct sets of rules under which politicians, bureaucrats, special interest group leaders, and journalists (the media) operate; the nature and scope of the bargaining that takes place between these groups of players; and the impact of information costs on voting behaviour.

Each of the four groups identified above consists of individuals who operate under a set of rules unique to itself. These sets of rules, which may be implicit as well as explicit, constitute the incentive system under which they play their own games of politics, bureaucracy, etc. It is assumed that all of the players seek to maximize their self-interest as they perceive it, and that behavioural differences among the players in different games are largely attributable to the fact that they are subject to different incentives. (Personnel selection standards and procedures are another possible explanation of intergroup behavioural differences, but this factor has not been examined here.) This analysis implies, of course, that to change the outcome of the expenditure budgetary process it would be necessary to change one or more of the four sets of rules that, to a large extent, determine what the players seek to achieve and to avoid in pursuing their self-interest.

While changes in the different incentives that direct the play in each of the four games certainly seem a necessary condition for changing the outcome of expenditure budgeting, they may not be sufficient. Endless bargaining goes on between teams. This bargaining goes on simultaneously on all six fronts (all combinations of pairs of the four games). The result of this bargaining, and it takes many forms, is partly dependent upon the strategic skills of the players. It also depends in part on what they have to bargain with – what might loosely be called their relative bargaining power. This implies that still another way to modify the outcome of the expenditure budgetary process would be to change the allocation of the bargaining chips held by the players in each of the several games.

This brings us to the question of information. As indicated earlier, control over information flows is an extremely important source of power in intergame bargaining (and intragame bargaining too, for that matter). For the present purpose, the impact of information costs on voting behaviour, and hence on budgetary decisions that are made to influence voting behaviour (or at least so as to not have an adverse effect upon it), is particularly relevant.

Much voting behaviour seems to be explicable in terms of the adoption of sets of voting decision rules by individuals in order to balance costs of making more informed voting decisions against the additional benefits they perceive as likely to accrue. It seems plausible that many voters have what we have termed a 'band of indifference' with respect to the effects of policy decisions upon themselves. As long as they *perceive* that actual or promised policies of the ministry, and the promised policies of opposition parties, would not likely produce results falling outside this band, the individual is unlikely to abandon his or her voting rule. This implies that a ministry will have a tendency to beggar its firm supporters up to the lower edge of this band of indifference and bonus marginal voters in marginal ridings. It also implies that a major problem, if not the primary problem, faced by opposition parties is one of credibility. They may make attractive promises that, if they were certain of implementation, would provide net benefits well above the band of indifference of a majority of voters. But these promises are likely to be heavily discounted - particularly when the past record of the ministry has not been so unfavourable as to trigger a reconsideration of the voting decision rules of its past supporters.

The next chapter attempts to spell out, in an admittedly impressionistic way, some of the questions that might be posed in attempting a rough list of these implications.

4
Towards some testable propositions

It is not possible to predict the precise outcome of the budgetary game, because there is so much room for strategic behaviour within complex sets of rules. The outcome depends largely on perceptions of perceptions rather than on 'facts.' Personalities are important. It may be possible, however, to set forth a few propositions that could be 'tested' in a non-rigorous way by undertaking a number of case studies of particular budgetary decisions.

The growth of the economy raises government tax revenues each year without changes in the tax laws.[1] This fiscal dividend, as it is sometimes called, is of crucial importance to a government because it is obtained at little or no political cost. Taxpayers, having capitalized existing taxes (adjusted their subjective net worth statements in our terminology), do not feel that their interests are being hurt. Even if they were aware that more revenues were being raised from them because of, say, the progressive rate schedule of the personal income tax, the increased bite is so gradual and so general that there is little basis for rallying opposition.

The same is true of borrowing that grows no more rapidly than the natural growth in revenues. These additional borrowed funds are, to all intents and purposes, politically costless. The sum of the additional funds obtained by increasing borrowing by this amount and the extra tax revenues can be termed a government's 'annual cash bonus.' It seems useful to take this bonus as the starting point. Given the decision rules just enunciated, when does it make sense for a

1 It should be recalled that this paper does not purport to deal with either substantial inflation or unemployment, which to a considerable extent change the usual rules.

government to increase expenditures by less than the annual bonus? or by more than the annual bonus? or to change the relative share of expenditures devoted to existing programs?

The first point to be made is that it is virtually impossible to reduce statutory benefits because they have been capitalized by the recipients and are thought of as benefits by right. Secondly, politicians seldom find it expedient to reduce departmental budgets to the point where present employees must be laid off, because of the perceived potential retaliation of the bureaucracy as a whole. Thirdly, some expenditures, important sources of income to private sector suppliers who are major employers in their areas or major party contributors, are also extremely painful to cut. Fourthly, some programs are symbolic in the sense that they show a concern for a problem. It is politically difficult, to say the least, to cut these programs because the problem is usually a matter of concern to swing voters.

With a growing population and economy the costs of providing most statutory benefits rise each year; even with modest inflation, wage budgets and contract prices also rise. This means, in effect, that unless an existing program can be cut without major political cost, a substantial part of the annual cash bonus is usually not available for discretionary disposition. This leads to the proposition that tax cuts will seldom be greater than a relatively small fraction of the cash bonus unless they can be offset by increases in borrowing greater than the natural growth of tax revenues.

Tax cuts are politically attractive under three circumstances. When it is necessary for a government to try to please a small minority group it is advantageous both to the government and to the members of the group to obtain the benefit by way of a tax concession rather than an expenditure increase. The present value of the concession is not obvious and, having been enacted, is not explicitly voted upon each year. Secondly, when a problem is so widespread that an expenditure program cannot be devised to assist all of those adversely affected (e.g. unemployment or inflation), a tax cut can serve a symbolic purpose by appearing to show concern. The amount of the cut need not be commensurate with the magnitude of the problem it purports to reduce or resolve. Finally, when a minister of finance wants to improve his public image at the expense of his colleagues he does so by pressing for reduced taxes rather than increased expenditures. He gains popularity by the former, they by the latter.

Let us now consider the other basic decision. Under what conditions are expenditures likely to rise faster than the natural growth of revenues? That is to say, when does it make sense for ministers to explicitly raise taxes or increase the rate of increase of borrowing? The formal answer is implicit in what has already been said. Governments will raise taxes or borrowing when the increase

in votes expected in swing ridings through the provision of the extra benefits is likely to exceed the number of votes expected to be lost by imposing the additional costs. If the costs can be allocated in such a way that voters in 'safe' and 'hopeless' ridings can be made to finance the extra benefits provided to swing voters in swing ridings the government of the day has it made. The trick is, of course, to follow one or all of the tactics previously described to avoid either alienating the committed voters in safe ridings so that they lose their commitment to the party in power or by alienating the voters in hopeless ridings committed to another party to the point where they are so desperate that they are willing to break the law.

This is all very well but hardly constitutes a set of testable hypotheses. The following propositions, while certainly not rigorously derived from this formal 'answer,' are perhaps capable of being examined qualitatively through case studies. It should be noted that they ignore the special cases of wars and major depressions or inflations that alter the usual rules.

1 With occasional minor aberrations related to economic stabilization problems, government expenditures will grow at least as fast as the annual cash bonus.

2 The lower the political cost of obtaining additional funds, as previously defined, the faster the rate of increase over and above the growth in the annual cash terms. It would be a major breakthrough to devise an operational definition of the political cost of funds.

3 Leaving aside capital expenditures and programs mounted to meet a temporary emergency that have not existed for more than a year or two,[2] expenditures on the vast majority of existing programs will not be reduced in *current dollar terms* in any one year.

4 Any reductions in real terms (a rare event) usually will not result in the dismissal of public servants in significant numbers or reduce the employment of suppliers in areas where unemployment is high. Contraction will be held to the natural attrition of staff.

5 The smaller the group to be benefited the more likely that it will be provided by non-expenditure means: by regulation, tax concessions, or loans.

6 The larger the group to be benefited the more likely that it will be provided by additional expenditures (again with the exception of small and often temporary tax cuts related to the existence of high rates of unemployment or inflation).

7 The greater the political power of the prime minister or the minister of finance relative to other ministers, the more slowly expenditures will rise.

8 While one would expect that the fastest rates of increase would occur when

2 Emergency measure programs that survive for more than two or three budgets are likely to be as permanent as the others!

unemployment is high, and conversely, it is doubtful that the difference is significant, because the extra revenues generated by inflation burn holes in the pockets of ministers that the minister of finance has not the power to repair.

9 Programs financed by earmarked taxes, fees, premiums, or contributions will grow more rapidly than those financed from general revenues, barring offsetting demographic changes.

10 The rate of growth of expenditures on programs that provide true public goods (e.g. defence, police, research) are likely to be determined by some kind of formula to reduce controversy within the system (e.g. foreign aid).

11 Government reorganizations will increase the expenditures on the affected programs.

12 Bureaucratic overhead will rise more rapidly than government expenditures generally.

13 Ministers require a number of expenditure programs that can be used to provide benefits on a highly discretionary basis to different groups of voters (the pork barrel). Because pork barrelling is not acceptable to voters who are not benefiting, new programs have to be created which have legitimacy for a time, and old programs of this type will be allowed to languish.

14 Expenditures on programs financed on a shared-cost basis will grow more rapidly than similar programs financed by one level of government. In part this is attributable to the alliances that arise between senior officials in the two levels of government responsible for the same field.

15 Contrary to some bureaucratic theories, under the parliamentary system the most prestigious employments are in departments with relatively small budgets. The deputy heads of these agencies do not want to maximize their budgets; they want to maximize their power and influence. They fight about their own budgets only to the extent that it affects the quantity and quality of their staff advisers relative to others with whom they compete.

16 Many of the changes in the relative shares of the ever-growing cash flow devoted to existing programs probably can be explained by 'errors,' New statutory programs are adopted or old programs revised with little understanding by the cabinet of the long-term cost implications - except by those who are advocating them.[3] Having pushed the legislation through, it is extremely difficult to control the escalation of costs because to do so would be an admission of error. The result is that other programs are squeezed, at least relatively.

17 The power and influence of the bureaucracy over the budget rests more in the suppression of information, particularly about alternatives, than in its ability to push through changes that ministers do not like.

3 An alternative explanation is that the problem arises not because ministers are unaware of the cost implications but because they discard them as too distant - not likely to have a significant impact before the next election.

18 One of the mysteries is the explanation of intergovernmental transfers. These transfers are extraordinarily valuable to the donee government but seem to have little political payoff to the donor government. Presumably the voter, simultaneously a resident of three jurisdictions, is persuaded by one of them that one or more of the others (the potential donor) is not acting in his interest. But, short of a constitutional referendum, the voter does not have a choice unless one of the parties operating in one jurisdiction clearly stands for shifting funds to another jurisdiction and makes this the cornerstone of its platform.

The next task, and it is an exceedingly difficult one because of government secrecy about the decision-making process, is to attempt to test these and similar hypotheses against what actually happened in particular cases. As stated earlier, it is unlikely that a rigorous model of the expenditure budgetary process possessing reliable predictive power can ever be developed, for to do so would mean an ability to forecast what turn out to be historic events. Nevertheless, it does not seem to be beyond the wit of man to obtain a much better understanding than we have now. A greater understanding could, at a minimum, reduce the time wasted tilting at windmills. Conceivably, it could have an impact on the decisions out of which history is made.

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5 A Theory of the Expenditure Budgetary Process

D.G. HARTLE

This crisp, provocative, lively, sometimes opinionated analysis is an important contribution to the scanty Canadian literature on the politics of the budgetary process. It is an important theoretical contribution to the study of political decision-making made by an economist.

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ISBN 0-8020-3341-5

University of Toronto Press